



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

April 28, 2008

Honorable Steven L. Beshear, Governor
Cabinet Secretaries and Agency Heads
Members of the Commonwealth of Kentucky Legislature

As Auditor of Public Accounts, I am pleased to transmit herewith our report of the Statewide Single Audit of the Commonwealth of Kentucky-Volume II for the year ended June 30, 2007. Beginning this year, our Statewide Single Audit of the Commonwealth of Kentucky report will be transmitted in two volumes in order to meet new reporting guidelines established by the American Institute of Certified Public Accountants. Volume I contains financial statement findings identified during our audit of the Comprehensive Annual Financial Report (CAFR), the Schedule of Expenditures of Federal Awards (SEFA), related notes, and our opinion thereon, as well as the Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*. Volume I was issued under a separate cover. Volume II contains the Report on Compliance With Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133, federal award findings and questioned costs identified during our audit, and the summary schedule of prior audit findings.

The Auditor of Public Accounts also calculates a dollar threshold, based on OMB Circular A-133 guidance, to determine the federal programs to be audited for internal controls and compliance. For FY 07, the threshold for auditing federal programs was \$21 million.

On behalf of the Office of Financial Audits of the Auditor of Public Accounts' Office, I wish to thank the employees of the Commonwealth for their cooperation during the course of our audit. Should you have any questions concerning this report, please contact Sally Hamilton, Executive Director, Office of Financial Audits, or me.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Crit Luallen".

Crit Luallen
Auditor of Public Accounts



**REPORT OF THE STATEWIDE SINGLE AUDIT OF THE
COMMONWEALTH OF KENTUCKY**

VOLUME II

**For the Year Ended
June 30, 2007**



**CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS
www.auditor.ky.gov**

**105 SEA HERO ROAD, SUITE 2
FRANKFORT, KY 40601
TELEPHONE (502) 573-0050
FACSIMILE (502) 573-0067**

CONTENTS

	<u>Page</u>
<u>INTRODUCTION</u>	
Single Audit.....	1
Schedule of Findings and Questioned Costs	1
Summary Schedule of Prior Audit Findings	2
Audit Approach	2
Component Units.....	2
List Of Abbreviations/Acronyms Used In This Report.....	4
<u>REPORT ON COMPLIANCE AND ON INTERNAL CONTROL</u>	
Report on Compliance With Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance With OMB Circular A-133	11
<u>SCHEDULE OF FINDINGS AND QUESTIONED COSTS</u>	
Section 1 - Summary of Auditor's Results	15
Section 2 - Financial Statement Findings	18
Financial Statement Findings 1 through 75 are provided in SSWAK Volume I.	
Section 3 - Federal Award Findings and Questioned Costs	
<u>Significant Deficiencies Relating to Internal Controls and/or Reportable Instances of Noncompliance:</u>	
<u>FINDING 07-CHFS-76:</u> The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Supporting Documentation.....	19
<u>FINDING 07-CHFS-77:</u> The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Documentation To Support IV-E Eligibility Determinations.....	22
<u>FINDING 07-CHFS-78:</u> The Cabinet For Health And Family Services Should Ensure Foster Parent Case Files Adhere To Title IV-E Regulations And Procedures For Foster Family Licensing.....	25
<u>FINDING 07-CHFS-79:</u> The Cabinet For Health And Family Services Should Ensure The CMS-64 Is Completely Reconciled Each Quarter	27

CONTENTS

(Continued)

Page

Section 3 - Federal Award Findings and Questioned Costs (Continued)

Significant Deficiencies Relating to Internal Controls and/or Reportable Instances of Noncompliance (Continued):

<u>FINDING 07-DMA-80:</u> The Department Of Military Affairs Should Implement Procedures To Ensure That All Subrecipients Are Monitored In Compliance With A-133 Requirements	31
<u>FINDING 07-DMA-81:</u> The Department Of Military Affairs Should Ensure That Subrecipient Grant Expenditures Meet The Requirements Of OMB Circular A-87	34
<u>FINDING 07-DMA-82:</u> The Department Of Military Affairs Should Immediately Develop Corrective Action Plans For Subrecipient Audit Findings And Resolve Questioned Costs	39
<u>FINDING 07-DMA-83:</u> The Department Of Military Affairs Should Submit Federal Reimbursements Timely	44
<u>FINDING 07-DWI-84:</u> The Department For Workforce Investment Should Ensure Activity Does Not Affect Closed Grants	47
<u>FINDING 07-EPPC-85:</u> The Division Of Forestry Needs To Communicate Federal Award Information To All Subrecipients	50
<u>FINDING 07-EPPC-86:</u> The Abandoned Mine Lands Should Make Timely Payments To Vendors	52
<u>FINDING 07-EPPC-87:</u> The Abandoned Mine Lands Subrecipients Required To Submit A-133 Reports Should Be Tracked	54
<u>FINDING 07-FAC-88:</u> The Finance And Administration Cabinet Should Improve Controls Related To The Cash Management Interest Liability Calculation To Ensure It Is Accurate.....	56
<u>FINDING 07-KOHS-89:</u> The Kentucky Office Of Homeland Security Should Improve Internal Controls Over The Preparation Of Its SF-269 Financial Status Report.....	61
<u>FINDING 07-TC-90:</u> The Kentucky Transportation Cabinet Should Ensure Federal Reports Are Accurately Prepared And Completely Supported	63

CONTENTS

(Continued)

	<u>Page</u>
Section 3 - Federal Award Findings and Questioned Costs (Continued)	
<u>Significant Deficiencies Relating to Internal Controls and/or Reportable Instances of Noncompliance (Continued):</u>	
<u>FINDING 07-TC-91:</u> The Kentucky Transportation Cabinet Should Ensure Independence With Right Of Way Employees, And Should Adhere To Established Procedures Regarding The Approval Process Of Right Of Way For State Employees	67
<u>Material Weaknesses and/or Material Instances of Noncompliance:</u>	
<u>FINDING 07-TC-92:</u> The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards	72
<u>FINDING 07-TC-93:</u> The Kentucky Transportation Cabinet Should Implement Policies And Procedures For Tracking Subrecipients' Audit Reports.....	80
<u>SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS</u>	85
<u>APPENDIX</u>	94

THIS PAGE LEFT BLANK INTENTIONALLY

INTRODUCTION

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2007**

Single Audit

The Auditor of Public Accounts (APA) annually performs a statewide single audit of the Commonwealth of Kentucky.

The APA prepares the Single Audit in compliance with Generally Accepted Auditing Standards, Generally Accepted Government Auditing Standards, and the requirements of Office of Management and Budget (OMB) Circular A-133. The APA, on behalf of the Commonwealth of Kentucky, also prepares a reporting package as required by OMB Circular A-133. The reporting package includes the basic financial statements, Schedule of Expenditures of Federal Awards (SEFA), auditor's reports, Schedule of Findings and Questioned Costs, and Summary Schedule of Prior Audit Findings. For the fiscal year ended June 30, 2007 (FY 07), the Single Audit is presented in two reports: the SSWAK Volume I and Volume II. In addition, the Comprehensive Annual Financial Report (CAFR), which has been issued under a separate cover, is included in the reporting package to present the basic financial statements and the auditor's report thereon.

SSWAK - Volume I contains financial reporting information based on our audit of the CAFR. It includes the APA's opinion on the Schedule of Expenditures of Federal Awards (SEFA) in relation to the financial statements, the *Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards*, and financial statement findings related to internal control and compliance.

SSWAK - Volume II presents elements required under OMB Circular A-133, including the *Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control over Compliance in Accordance with OMB Circular A-133*, the Schedule of Findings and Questioned Costs, and the Summary Schedule of Prior Audit Findings.

Schedule of Findings and Questioned Costs

The Schedule of Findings and Questioned Costs consists of three sections: Summary of Auditor's Results, Financial Statement Findings, and Federal Award Findings and Questioned Costs. The Summary of Auditor's Results summarizes the type of audit reports issued and lists major programs audited. The Federal Award Findings and Questioned Costs lists all findings related to federal awards. In both sections, significant deficiencies and reportable instances of noncompliance are presented first, then material weaknesses and material instances of noncompliance.

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Summary Schedule of Prior Audit Findings

Audit findings related to federal awards reported in the Schedule of Findings and Questioned Costs for FY 06, as well as any previous federal awards findings that have not been resolved, are reported in the Summary Schedule of Prior Audit Findings for FY 07.

The Summary Schedule of Prior Audit Findings is organized based on whether the prior audit finding was a significant deficiency or a material weakness or noncompliance. The findings of each classification (significant deficiency, material weakness or noncompliance) are categorized as (1) fully corrected, (2) not corrected or partially corrected, (3) corrective action taken differs significantly from corrective action previously reported, or (4) finding no longer valid or does not warrant further action.

Audit Approach

The scope of the statewide single audit for FY 07 included:

Financial

- An audit of the basic financial statements and combining financial statements;
- Limited procedures applied to required supplementary information;
- An audit of the SEFA sufficient to give an opinion in relation to the basic financial statements;
- Tests of compliance with certain provisions of laws, regulations, contracts, and grants, and tests of internal controls, where applicable;
- Findings related to internal control and compliance over financial reporting, when noted during the audit of the CAFR.

Federal Awards

- An audit of compliance with the compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* applicable to each major federal program; and
- Tests of internal control over compliance in accordance with OMB Circular A-133.

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Component Units

The Single Audit Act Amendments permit the single audit to cover the entire operations of the entity or include a series of audits covering departments, agencies, or other organizational units expending federal awards. The Commonwealth has elected to exclude discretely presented component units from the statewide single audit, except as part of the audit of the basic financial statements. Thus, discretely presented component units are not included in the report on compliance and internal control and corresponding Schedule of Findings and Questioned Costs. It should be noted, however, that these entities are still required to have audits performed in accordance with the provisions of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, if applicable.

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report

AIOM	Air Operations and Maintenance
AML	Abandoned Mine Lands
AMLR	Abandoned Mine Lands Reclamation
APA	Auditor of Public Accounts
BCCTP	Breast and Cervical Cancer Treatment Program
CAFR	Comprehensive Annual Financial Report
CAR	Consolidated Annual Financial Report
CBW	Child Benefits Worker
CFC	Cabinet for Families and Children
CFDA	Catalog of Federal Domestic Assistance
CFR	Code of Federal Regulations
CHFS	Cabinet for Health and Family Services
CMIA	Cash Management Information System
CMS	Centers for Medicaid Services
Commonwealth	Commonwealth of Kentucky
CPA	Certified Public Accountant
CPG	Consolidated Payment Program
CR	Cash Receipt
CSEPP	Chemical Stockpile Emergency Preparedness Program
D.C.	District of Columbia
DCBS	Department of Child Benefits Services
DMA	Department of Military Affairs
DMS	Department for Medicaid Services
DOF	Division of Forestry
DPREC	Deposit Reconciliation Table
DVOP	Disabled Veterans' Outreach Program
DWI	Department for Workforce Investment
EDS	Electronic Data Systems
EMARS	Enhanced Management Administrative Reporting System
EPPC	Environmental and Public Protection Cabinet
FAC	Finance and Administration Cabinet
FEMA	Federal Emergency Management Administration
FFP	Federal Financial Participation
FFY	Federal Fiscal Year
FHWA	Federal Highway Administration
FPM	Federal Program Manager
FY	Fiscal Year
HS	Highway Safety
IPT	Integrated Process Team

**COMMONWEALTH OF KENTUCKY
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

List Of Abbreviations/Acronyms Used In This Report (Continued)

JE	Journal Entry
JUST	Justice Cabinet
JV	Journal Voucher
JVE	Journal Voucher Entry
KAR	Kentucky Administrative Regulation
KOHS	Kentucky Office of Homeland Security
KRS	Kentucky Revised Statute
KSP	Kentucky State Police
KY	Kentucky
KyDEM	Kentucky Division of Emergency Management
KYTC	Kentucky Transportation Cabinet
LPA	Local Public Agencies
MARS	Management Administrative Reporting System
MMIS	Medicaid Management Information System
MOA	Master Agreement
MPO	Metropolitan Planning Organization
NHTSA	National Highway Transportation Safety Administration
No.	Number
O & M	Operations and Maintenance
OFS	Office of Fiscal Services
OIG	Office of Inspector General
OMA	Office of Management and Administration
OMB	Office of Management and Budget
OVAE	Office of Vocational and Adult Education
PDF	Portable Document Format
PRC	Commodity Based Purchase Request
R & D	Research and Development
ROW	Right of Way
SEFA	Schedule of Expenditures of Federal Awards
SF	Short Form
SSWAK	Statewide Single Audit of the Commonwealth of Kentucky
TC	Transportation Cabinet
TE	Transportation Enhancement
UASI	Urban Areas Security Initiative
U.S.	United States
U.S. DHHS	United States Department of Health and Human Services
U.S. DOE	United States Department of Education
USFPO	United States Fiscal and Property Officer
WIA	Workforce Investment Act

THIS PAGE LEFT BLANK INTENTIONALLY

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL



CRIT LUALLEN
AUDITOR OF PUBLIC ACCOUNTS

Honorable Steven L. Beshear, Governor
Cabinet Secretaries and Agency Heads
Members of the Commonwealth of Kentucky Legislature

Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133

Compliance

We have audited the compliance of the Commonwealth of Kentucky with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2007.

The Commonwealth's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the Commonwealth's management. Our responsibility is to express an opinion on the Commonwealth's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Commonwealth's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Commonwealth's compliance with those requirements.



Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133
(Continued)

As described in items 07-TC-92 and 07-TC-93, in the accompanying schedule of findings and questioned costs, the Transportation Cabinet, an agency of the Commonwealth, did not comply with requirements regarding subrecipient monitoring that are applicable to the Highway Planning and Construction program (CFDA 20.205) and the Highway Safety program (CFDA 20.600). Compliance with such requirements is necessary, in our opinion, for the Commonwealth to comply with the requirements applicable to those programs.

In our opinion, except for the instances of noncompliance described in the preceding paragraph, the Commonwealth complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2007. However, the results of our auditing procedures disclosed other instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 07-CHFS-79, 07-DMA-80, 07-DMA-81, 07-DMA-82, 07-EPPC-85, 07-EPPC-87, and 07-TC-90.

Internal Control Over Compliance

The management of the Commonwealth is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Commonwealth's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

A control deficiency in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that a noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the

Report on Compliance With Requirements Applicable to Each
Major Program and on Internal Control Over Compliance in
Accordance With OMB Circular A-133
(Continued)

entity's internal control. We consider the deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs as items 07-CHFS-76, 07-CHFS-77, 07-CHFS-78, 07-CHFS-79, 07-DMA-80, 07-DMA-81, 07-DMA-82, 07-DMA-83, 07-DWI-84, 07-EPPC-86, 07-FAC-88, 07-KOHS-89, 07-TC-90, 07-TC-91, 07-TC-92, and 07-TC-93 to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. Of the significant deficiencies in internal control over compliance described in the accompanying schedule of findings and questioned costs, we consider items 07-TC-92 and 07-TC-93 to be material weaknesses.

We also noted certain immaterial instances of noncompliance and other matters involving internal control over compliance, which we have communicated to management in a separate letter.

Management's responses to the findings identified in our audit are included in the accompanying schedule of findings and questioned costs. We did not audit their responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the management, members of the legislature, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

A handwritten signature in black ink, appearing to read 'Crit Luallen', with a stylized, cursive script.

Crit Luallen
Auditor of Public Accounts

March 24, 2008

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007**

SECTION 1 - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Financial Statements: We issued an unqualified opinion on the governmental activities, business type activities, aggregate discretely presented component units, each major fund, and aggregate remaining fund information of the Commonwealth for the year ended June 30, 2007.

Compliance: In relation to the audit of the basic financial statements of the Commonwealth, the results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting: Our consideration of the Commonwealth's internal control over financial reporting disclosed 75 significant deficiencies. We believe two (2) of the significant deficiencies of internal control over financial reporting to be material weaknesses.

Federal Awards

Compliance: We issued a qualified opinion on the Commonwealth's compliance with the requirements applicable to each of its major federal programs. The results of our auditing procedures disclosed nine instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133. We believe two of the instances of noncompliance are material.

Internal Control Over Compliance: Our consideration of the Commonwealth's internal control over compliance disclosed 18 significant deficiencies. We believe that two of the significant deficiencies are material weaknesses.

Identification of Major Programs

The following is a list of major Type A programs:

CFDA #	Program Title
10.557	Special Supplement Nutrition Program for Women, Infants and Children
Workforce Investment Act Cluster:	
17.258	WIA Adult Program
17.259	WIA Youth Activities
17.260	WIA Dislocated Workers
20.205	Highway Planning and Construction

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 1 - SUMMARY OF AUDITOR'S RESULTS (CONTINUED)

Identification of Major Programs (Continued)

The following is a list of major Type A programs (Continued):

CFDA #	Program Title
93.558	Temporary Assistance for Needy Families
93.563	Child Support Enforcement
Child Care Cluster:	
93.575	Child Care and Development Block Grant
93.596	Child Care Mandatory and Matching Funds of the Child Care and Development Fund
93.658	Foster Care-Title IV-E
93.659	Adoption Assistance
93.767	State Children's Insurance Program
Medicaid Cluster:	
93.775	State Medicaid Fraud Control Units
93.777	State Survey and Certification of Health Care Providers and Suppliers
93.778	Medical Assistance Program
Homeland Security Cluster:	
97.004	State Domestic Preparedness Equipment Support Program
97.067	Homeland Security Grant Program

The following is a list of major Type B programs:

CFDA #	Program Title
10.664	Cooperative Forestry Assistance
12.401	National Guard Military Operations and Maintenance (O & M) Projects
15.250	Regulation of Surface Coal Mining
15.252	Abandoned Mine Land Reclamation (AMLR) Program
Fish and Wildlife Cluster:	
15.605	Sport Fish Restoration
15.611	Wildlife Restoration

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 1 - SUMMARY OF AUDITOR'S RESULTS (CONTINUED)

Identification of Major Programs (Continued)

The following is a list of major Type B programs (Continued):

CFDA #	Program Title
Employment Services Cluster:	
17.207	Employment Service
17.801	Disabled Veterans' Outreach Program (DVOP)
17.804	Local Veterans' Employment Representative Program
20.509	Formula Grants for Other Than Urbanized Areas
Highway Safety Cluster:	
20.600	State And Community Highway Safety
20.601	Alcohol Traffic Safety and Drunk Driving Prevention Incentive Grants
66.460	Nonpoint Source Implementation Grants
84.048	Vocational Education-Basic Grants to States
84.287	Twenty-First Century Community Learning Centers
84.357	Reading First State Grants
97.008	Urban Areas Security Initiative
97.036	Public Assistance Grants

Dollar Threshold Used to Distinguish Between Type A and Type B Programs

The maximum dollar threshold used to distinguish between Type A and Type B Programs was \$21 million.

Auditee Risk

The Commonwealth did not qualify as a low-risk auditee.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 2 - FINANCIAL STATEMENT FINDINGS

See SSWAK Volume I for the FY 07 Financial Statement Findings 1 through 75.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

*Significant Deficiencies Relating to Internal Controls and/or
Reportable Instances of Noncompliance:*

FINDING 07-CHFS-76: The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Supporting Documentation

State Agency: Cabinet for Health and Family Services
Federal Program: CFDA 93.658 - Foster Care- Title IV- E
CFDA 93.659 - Adoption Assistance
Federal Agency: U.S. Department of Health and Human Services
Pass-Through Agency: Not Applicable
Compliance Area: Activities Allowed or Unallowed, Eligibility
Amount of Questioned Costs: \$0

During audit testing for the Title IV-E Grant, we selected 80 Foster Care/Adoption Assistance cases to be reviewed at the DCBS offices located in the following counties: Scott, Fayette, Jefferson, and Christian. Out of 80 cases tested, we noted four (4) missing case files. In all instances, the case file was missing at the time of testing. The exceptions are as follows:

- Jefferson County had one (1) missing IV-E file for Foster Care.
- Jefferson County had one (1) missing case file for Adoption Assistance that was destroyed in 2001. No replacement file for 2001-2007 subsidy payments.
- Jefferson County had two (2) missing IV-E files for Adoption Assistance.

During audit testing, we selected 80 cases subject to a federal eligibility test. Of the 80 cases selected, the auditor was not provided supporting documentation pertaining to the federal eligibility test for four (4) cases. Since the auditor was not provided documentation for 4 of the 80 cases selected, it cannot be determined if the state is in compliance with federal requirements regarding the eligibility of foster care and adoption assistance for Title IV-E.

Local offices did not adhere to Cabinet for Health and Family Services (CHFS) Title IV-E regulations and procedures and case files were not tracked and filed appropriately to prevent loss.

When Title IV-E regulations and procedures are not adhered to, CHFS cannot be assured that expenditures are being made appropriately and to eligible foster/adoptive parents or childcare providers. When Foster Care or Adoption Assistance case records are not maintained or are missing, we cannot review the child's information and documentation

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-76: The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Supporting Documentation (Continued)

for IV-E eligibility. In addition, if DCBS offices do not maintain adequate case records, the Cabinet for Health and Family Services and the U.S. Department of Health and Human Services cannot be assured that benefits are issued to eligible recipients. This could result in the DHHS assessing a penalty against CHFS.

Per 45 Code of Federal Regulation (CFR) 1356.21(b) IV-E agencies are required to show that reasonable efforts were made to prevent the child's removal from the home. This involves the establishment of a judicial determination of reasonable efforts to prevent a child's removal from the home.

45 CFR 1356.71(f) requires the case record of the child to contain sufficient documentation to verify a child's eligibility.

Recommendation

We recommend Title IV-E regulations and procedures be adhered to before Federal funds are expended. We recommend CHFS provide additional training to its Social Workers, Billing Specialists, and Child Benefits Worker (CBW) to ensure all regulations and procedures are followed and required timeframes are met.

Case files should be maintained to adequately support eligibility and expenditures. CHFS should work with local offices to assist them in developing and maintaining an adequate filing system so case files can be tracked and located.

The missing case files, which have not been timely reconstructed, raises concerns regarding questioned costs in previous years for these cases. We are recommending the U.S. DHHS review the matter to determine if the lack of timely agency corrective action warrants further audit questioned costs.

Management's Response and Corrective Action Plan

Three of the four cases have been reconstructed since the audit. The CBW who was in charge of pulling together the cases for the audit had never done so before. She wasn't aware that she could reconstruct an IV-E case for an audit. The fourth adoption case was prior to the implementation of adoption cases in TWIST and the IV-E case couldn't be recreated. The adoption wasn't an IV-E adoption.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-76: The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Supporting Documentation (Continued)

Management's Response and Corrective Action Plan (Continued)

Management agrees that additional training is needed in this area. An adoption report will be generated and the CBW's will cross reference their files with the report to ensure they have the complete IV-E file. Also each month when the CBW completes a recertification for Medicaid on adoption cases they will review the adoption case and make sure they have all the updated information that is required in the case, if they do not, they will request the information from the appropriate worker. CBW will make sure that all signatures and rates are listed on the contracts. Management will complete reviews of adoption subsidy cases periodically to ensure staff is completing cases correctly and that all documentation is in the case. Management will also compile all case reviews to see where there is a need for training.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-77: The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Documentation To Support IV-E Eligibility Determinations

State Agency: Cabinet for Health and Family Services

Federal Program: CFDA 93.658 - Foster Care- Title IV- E

CFDA 93.659 - Adoption Assistance

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Eligibility

Amount of Questioned Costs: \$0

During audit testing for the Title IV-E Grant, we selected 80 Foster Care/Adoption Assistance cases to be reviewed at the DCBS offices located in the following counties: Scott, Fayette, Jefferson, and Christian. Out of 80 cases tested, we noted two (2) exceptions. Two (2) exceptions, both from Christian County, were noted as follows:

- One (1) child not determined for IV-E status.
- One (1) child not determined for IV-E and no court order obtained for removal from home.

During audit testing, we selected 80 cases subject to a federal eligibility test. Of the 80 cases selected, the auditor was not provided supporting documentation pertaining to the federal eligibility test for two (2) cases. Since the auditor was not provided documentation for 2 of the 80 cases selected, it cannot be determined if the state is in compliance with federal requirements regarding the eligibility of foster care and adoption assistance for Title IV-E.

The proper documentation was not obtained from the agency and filed in the case folder.

When Title IV-E regulations and procedures are not adhered to, CHFS cannot be assured that expenditures are being made appropriately and to eligible foster/adoptive parents or childcare providers. When Foster Care or Adoption Assistance case records are not maintained or are missing, we cannot review the child's information and documentation for IV-E eligibility. In addition, if DCBS offices do not maintain adequate case records, the Cabinet for Health and Family Services and the U.S. Department of Health and Human Services (U.S. DHHS) cannot be assured that benefits are issued to eligible recipients. This could result in the U.S. DHHS assessing a penalty against CHFS.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-77: The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Documentation To Support IV-E Eligibility Determinations (Continued)

Per 45 CFR 1356.21(b) IV-E agencies are required to show that reasonable efforts were made to prevent the child's removal from the home. This involves the establishment of a judicial determination of reasonable efforts to prevent a child's removal from the home.

45 CFR 1356.71(f) requires the case record of the child to contain sufficient documentation to verify a child's eligibility.

Recommendation

In general, we recommend Title IV-E regulations and procedures be adhered to before Federal funds are expended. We recommend CHFS provide additional training to its Social Workers, Billing Specialists, and Child Benefits Workers to ensure all regulations and procedures are followed and required timeframes are met.

Case files should be maintained to adequately support eligibility and expenditures. CHFS should work with local offices to assist them in developing and maintaining an adequate filing system so that case files can be tracked and located easily.

Management's Response and Corrective Action Plan

Both of these children were in state custody less than three days. The first child was in foster care 7-5-06 to 7-6-06; the second child was in care 8-13-06 to 8-15-06. This CBW was not notified of the removal of the first child. Since social workers were completing the placement screens in 2006, the child was entered and exited within a couple of days, and did not appear on the weekly CHIPS report.

This CBW was notified of the removal of the second child, however, policy at the time (2006), was to complete a Title IV-E determination if possible, but it was not necessary.

It may be noted that both of these children would not have been Title IV-E eligible as their families were military and their income would have made them ineligible

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-77: The Cabinet For Health And Family Services Should Ensure Adoption Assistance And Foster Care Case Files Have Documentation To Support IV-E Eligibility Determinations (Continued)

Management's Response and Corrective Action Plan (Continued)

on need. This CBW now does complete a Title IV-E determination on every child that is in CHFS custody, assuming she is notified of the removal.

Each month as the CBW completes the Medicaid recertification on adoption cases a review will be completed on the case to ensure all the updated information required is found in the case file. If they do not, they will request the information from the appropriate worker. CBW will make sure that all signatures and rates are listed on the contracts. Management will complete reviews of adoption subsidy cases periodically to ensure staff is completing cases correctly and that all documentation is in the case. Management will also compile all case reviews to verify training needs.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-78: The Cabinet For Health And Family Services Should Ensure Foster Parent Case Files Adhere To Title IV-E Regulations And Procedures For Foster Family Licensing

State Agency: Cabinet for Health and Family Services

Federal Program: CFDA 93.658 - Foster Care- Title IV- E

CFDA 93.659 - Adoption Assistance

Federal Agency: U.S. Department of Health and Human Services

Pass-Through Agency: Not Applicable

Compliance Area: Eligibility

Amount of Questioned Costs: \$0

During audit testing for Foster Parent Eligibility, we selected sixty (60) Foster Parent (Provider) cases to be reviewed at the DCBS offices located in the following counties: Scott, Fayette, Jefferson, and Christian. Out of 60 cases tested, we noted ten exceptions. The exceptions are as follows:

- Four (4) foster parent cases were missing current criminal record checks.
- Two (2) foster parent cases were missing the re-approval letter.
- Three (3) foster parents were short on training hours for FY07.
- One (1) foster parent is continually short on training hours each year. They were short one hour on their initial thirty training hours.

Local offices did not adhere to CHFS Title IV-E regulations and procedures for Foster Family licensing.

When Title IV-E regulations and procedures are not adhered to, CHFS cannot be assured that expenditures are being made appropriately to eligible foster/adoptive parents or childcare providers. When Foster Parents (Provider) case records are not maintained, we cannot review the Foster Parents information and documentation for IV-E eligibility. In addition, if DCBS offices do not maintain adequate case records, CHFS and the U.S. Department of Health and Human Services cannot be assured that benefits are issued to eligible recipients.

922 Kentucky Administrative Regulation (KAR) 1:490

Section 6. Reevaluation.

- (1) An approved foster or adoptive parent and each adult member of the household shall submit annually, prior to or during the anniversary month of initial approval, to a: (a) Criminal records check; and (b) Child abuse or neglect check conducted by the cabinet.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-78: The Cabinet For Health And Family Services Should Ensure Foster Parent Case Files Adhere To Title IV-E Regulations And Procedures For Foster Family Licensing (Continued)

(2) If an adult becomes a new member of an approved foster or adoptive parent's household, the new adult member of the household shall submit to background checks within thirty (30) calendar days of residence within the household in accordance with Section 2(1)(a) through (c) of this administrative regulation.

(3) If an adolescent becomes a new member of an approved foster or adoptive parent's household, the new adolescent member of the household shall submit to a child abuse and neglect check conducted by the Cabinet within thirty (30) calendar days of residence within the household.

922 KAR 1:350

Section 9. Preparation and Selection of a Resource Home Parent.

(2) A resource home applicant shall complete a: (a) Minimum of thirty (30) hours of initial family preparation

Section 15. Annual Resource Home Training Requirement.

(1)(a) A resource home parent shall be required to complete, before the anniversary date of approval, at least six (6) hours of annual cabinet-sponsored training or training approved in advance by the cabinet.

Recommendation

We recommend Title IV-E regulations and procedures be adhered to before Federal funds are expended. We recommend CHFS provide additional training to its Social Workers, Billing Specialists, and Child Benefits Workers to ensure all regulations and procedures are followed and required timeframes are met.

Case files should be adequately maintained to support Foster Parent eligibility.

Management's Response and Corrective Action Plan

Case management of Foster Homes and Adoptive Homes falls under the Division of Service Regions responsibility. They are responsible for ensuring training requirements, criminal record checks and approval letters are completed for the Foster and Adoptive Homes. The Division of Administration and Financial Management was able to obtain some of the missing information.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-79: The Cabinet For Health And Family Services Should Ensure The CMS-64 Is Completely Reconciled Each Quarter

State Agency: Cabinet for Health and Family Services
Federal Program: CFDA 93.778 - Medical Assistance Program
Federal Agency: U.S. Department of Health and Human Services
Pass-Through Agency: Not Applicable
Compliance Area: Reporting
Amount of Questioned Costs: \$0

During the CHFS audit, we discovered the Department for Medicaid Services (DMS) had brought a new Medicaid Management Information System (MMIS) into production. In performing our audit work, we discovered that as of December 20th, 2007 CHFS had not reconciled Medicaid expenditures in the amount of \$1,041,879,904 reported from Electronic Data Systems (EDS) with the statewide accounting and reporting system - Electronic Management Administrative Reporting System (eMARS), for the quarter ending June 30, 2007. CHFS uses the Centers for Medicare and Medicaid Services (CMS-64) for the Medical Assistance Program to report their actual program benefit costs and administrative expenses to CMS. CMS uses this information to compute the Federal financial participation rate for Kentucky's Medicaid program costs.

The Auditor inquired with CHFS about the following but CHFS never replied

- Were any contract provisions broken?
- Were any penalties assessed to EDS?
- Was CMS aware of the situation?
- Will CMS impose any penalties upon CHFS for not providing the CMS 64 in a timely manner?

Again, CHFS did not reply to the auditors questions. If CHFS DMS is paying for services not rendered, this would not be a good business practice nor in the best interest of the taxpayers.

CHFS is not reconciling the CMS 64 in the prescribed time frame due to EDS not providing the information needed for the reconciliation in a timely manner.

The CMS-64, *Quarterly Statement of Expenditures for the Medical Assistance Program* (OMB No. 0938-0067) for the quarter ending June 30, 2007 has not been reconciled.

By not submitting the reconciliation timely, CHFS cannot provide assurance that program expenditures were reasonable and necessary. Furthermore, CHFS is not in compliance with Federal Regulations.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-CHFS-79: The Cabinet For Health And Family Services Should Ensure The CMS-64 Is Completely Reconciled Each Quarter (Continued)

In accordance with the OMB Circular A-133, Compliance Supplement, the CMS-64, *Quarterly Statement of Expenditures for the Medical Assistance Program (OMB No. 0938-0067)* is required to be prepared quarterly and submitted electronically to CMS within 30 days after the end of the quarter. The amounts reported on the CMS-64 and its attachments must be actual expenditures for which all supporting documentation, in readily reviewable form, has been compiled and is available immediately at the time the claim is filed.

OMB Circular A-133 Compliance Supplement – Part 6 on internal control over Federal awards requires state agencies to monitor and document contractor performance with the terms, conditions, and specifications of the contract. Management should conduct independent reviews of procurements and contracting activities to determine whether policies and procedures are being followed as intended. Procedures should be sufficient to identify risks arising from vendor inadequacy.

Recommendation

We recommend CHFS reconcile Medical Assistance Program expenditures reported in the CMS-64, *Quarterly Statement of Expenditures for the Medical Assistance Program (OMB No. 0938-0067)* to eMARS within 30 days after the end of the quarter.

Also we recommend, CHFS DMS either setup monetary sanctions for EDS when services are not rendered, or reduce payment amounts, so the taxpayers are not paying for services not received.

Management's Response and Corrective Action Plan

The DMS response to the auditor's finding that DMS did not reconcile \$1,041,879,904 Medicaid expenditures for the quarter ending June 30, 2007, is provided and DMS total gross dollar reconciliation was in place. Each quarter, the Office of Fiscal Services (OFS), prepares the CMS 64 report for DMS, reconciles expenditures reported on the CMS 64 by comparing MMIS cycle data from EDS to the actual checkwriter files within eMARS. OFS staff prepares internal worksheets to compare and track data received and have created a check and balance process to systematically identify areas that do not reconcile.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 07-CHFS-79: The Cabinet For Health And Family Services Should
Ensure The CMS-64 Is Completely Reconciled Each Quarter (Continued)**

Management's Response and Corrective Action Plan (Continued)

The missing information pertains to two reports unavailable at time of filing from EDS. These reports list expenditures for two programs, Breast and Cervical Cancer Treatment Program (BCCTP) and Family Planning and Sterilization which receive a higher Federal Financial Participation (FFP) than the normal funding rate. When the CMS 64 report is prepared, the total Medicaid expenditures are reported for the quarter and bucketed into the appropriate FFP column. OFS staff had reconciled total expenditures between the MMIS and eMARS but had not received the reports to identify how much of those dollars reported at the regular FFP should be recorded within a different FFP column.

EDS has several performance measures to meet within numerous areas of operation. Monthly reviews are performed by DMS staff based upon report card criteria established quarterly. If EDS does not perform satisfactorily within those performance measures, penalties are assessed. DMS has assessed EDS certain penalties based upon performance and is reviewing additional ones. However, future penalties are contingent upon EDS' continued improvement and cooperative actions maintained.

DMS and OFS have been in contact with CMS since July when CHFS staff knew the CMS 64 reporting deadline would not be met and have continued to inform CMS of updates as they occur. The original plan with CMS was to not report BCCTP and Family Planning and Sterilization expenditures until the reports received were accurate, therefore OFS staff did not finalize their worksheets because that information was still pending. Since EDS has still failed to produce the reports accurately, CHFS staff have agreed to close and finalize the June 30, 2007 CMS 64 report at CMS' request and file a prior period adjustment on a future CMS 64 report when the reports are received from EDS.

Once the CMS 64 report is certified (submitted) by OFS, CMS performs a review to determine if there are any adjustments to be made based upon the original amount of federal funds requested for the quarter in comparison to the actual expenditures. Normally this process takes a couple of quarters to finalize at which time CMS will either award additional funds to DMS if expenditures were more than originally requested or take back the federal funds not spent. Although CMS does not impose penalties for reporting delays, there are losses to DMS

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 07-CHFS-79: The Cabinet For Health And Family Services Should
Ensure The CMS-64 Is Completely Reconciled Each Quarter (Continued)**

Management's Response and Corrective Action Plan (Continued)

because CMS can not finalize the CMS 64 report until the report is filed and closed which in turn can cause future funding delays. In addition, since the two reports not received yet are relating to enhanced FFP, DMS is being penalized by not being able to receive additional federal funds that would normally be claimed by these program expenditures.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-80: The Department Of Military Affairs Should Implement Procedures To Ensure That All Subrecipients Are Monitored In Compliance With A-133 Requirements

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 - Disaster Grants-Public Assistance (Presidentially Declared Disasters)

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: \$0

The Kentucky Emergency Management Division (KyDEM) of the Kentucky Department of Military Affairs (DMA) did not comply with the requirement to ensure all subrecipients receiving \$500,000 or more in federal aid obtained a single audit as provided in OMB Circular A-133. From a sample of twenty Public Assistance applicants, six were not asked to certify whether or not they were required to have a single audit. KyDEM also failed to follow up with four other applicants that did not respond to a letter requesting that certification.

In addition, one applicant (a county fiscal court) certified that it was not required to obtain a single audit because its total federal aid was under \$500,000. This certification was false, and in fact the county did obtain a single audit. KyDEM did not discover this, so it did not acquire or review a copy of the applicant's single audit.

A review of the subrecipient monitoring files and checklist indicated that KyDEM's internal auditor sent letters asking applicants to certify their single audit status during October through December 2006. However, the list of applicants was incomplete, so some did not receive a letter. The internal auditor subsequently left KyDEM, and no follow-up on single audits was performed after that date.

OMB Circular A-133 Subpart D states in part:

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:

...

- (4) Ensure that subrecipients expending \$300,000 (*\$500,000 for fiscal years ending after December 31, 2003*) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.

The audit requirement referred to is a single audit.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-80: The Department Of Military Affairs Should Implement Procedures To Ensure That All Subrecipients Are Monitored In Compliance With A-133 Requirements (Continued)

Recommendation

The DMA Division of Emergency Management should implement procedures to ensure that all subrecipients are properly monitored, including providing single audits for review when applicable. In order to carry out these procedures, the agency should consider assigning responsibility for monitoring single audit status to a permanent employee.

Management's Response and Corrective Action Plan

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for subrecipient monitoring is to provide reasonable assurance that Federal grant award information and compliance requirements are identified to subrecipients, subrecipient activities are monitored, subrecipient audit findings are resolved, the impact of any subrecipient noncompliance on the pass-through entity is evaluated, and subrecipients obtained required audits and take appropriate corrective action on audit findings. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance. The Federal Disaster Public Assistance Program had previously hired a position to monitor single audit reviews, but unfortunately lost the employee due to his transfer to another state agency. At that time, it became evident that the funds for this position could no longer support this salary and we were unable to backfill the position. The Kentucky Division of Emergency Management (KyDEM) is expecting a large number of their personnel to retire this year and to have large payouts for retirees. Because of these high payouts and the recent cap reductions in personnel, it will be difficult to hire or assign a position full-time to monitor the status of divisional internal control activities and processes during this federal fiscal year. As the budget permits and as a position becomes available, an Internal Auditor position will be included in the budget request in the Emergency Management Program Grant application for Federal FY 2009/2010 to monitor all federal grant activity for KyDEM.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-80: The Department Of Military Affairs Should Implement Procedures To Ensure That All Subrecipients Are Monitored In Compliance With A-133 Requirements (Continued)

Management's Response and Corrective Action Plan (Continued)

The core intent of this plan is to insure that this corrective action places the right people into the right job with the right skills and the right supervision to insure that this material misstatement does not occur again.

ACTION PLAN:

- (1) By April 15, 2008, KyDEM shall revise the current internal division policy #133-1 Subrecipient Audits / Monitoring established in 2004 to be further detailed to assure more in depth internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations.*
- (2) By May 30, 2008, training will be conducted with all concerned KyDEM personnel on the revised policy.*
- (3) Effective July 1, 2008, each KyDEM section responsible for the dispersion of federal grant funds shall review the audits for their federal program subrecipients, when received, to comply with OMB Circular A-133 and division policy #133-1 or later approved version. A memo of record of this review shall be provided to the pre-audit section for review. The Pre-Audit Section will have a checklist to assure paperwork is completed before giving to the Assistant Director for his/her review of each subrecipient reviewed.*
- (4) Each KyDEM section responsible for the dispersion of federal grant funds shall reconcile the amount of the Federal awards reported in subrecipient audit reports and to work with the subrecipients to resolve audit findings within six months after receipt of the subrecipient audit report and ensure the subrecipient takes timely corrective action.*

SUMMARY:

Until a position and funds become available, revising the current procedures and adding the separation of duties in the subrecipient monitoring review in this action plan will allow for better internal control and ensure the subrecipient's reviews are followed through for completion.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-81: The Department Of Military Affairs Should Ensure That Subrecipient Grant Expenditures Meet The Requirements Of OMB Circular A-87

State Agency: Department of Military Affairs

Federal Program: CFDA 97.040 - Chemical Stockpile Emergency Preparedness Program

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Allowable Costs/Cost Principles

Amount of Questioned Costs: \$9,952

We received an allegation of questionable federal charges related to the Chemical Stockpile Emergency Preparedness Program (CSEPP) that arose during a fiscal court audit. The auditor found a check in the amount of \$11,136 paid to the county's CSEPP coordinator to reimburse him for the buy-back of prior service credits from the Kentucky Retirement System for time worked in another position in the early 1980's, and noted that the county was reimbursed \$9,952 of this expenditure through the CSEPP program.

The purpose of the CSEPP program is to improve emergency preparedness in 10 Kentucky counties in the event that an accident would occur at the Bluegrass Army Depot. The program goes through a regimented budget process each year. Each county proposes a budget for personnel, equipment, training, and other grant-related items. The state CSEPP program manager reviews the request initially and recommends or denies each line item according to allowable costs under the program. Those items approved by the state are then reviewed and approved by a Regional Federal Emergency Management Administration (FEMA) representative and ultimately by a representative from the FEMA headquarters in Washington, D.C.

The Department of Military Affairs (DMA) administers the CSEPP grant in Kentucky. Although this grant was not identified as a major federal program for FY 2007, the auditor determined that an investigation was warranted since it appears that not only did the county approve this expenditure, but it was also approved by state CSEPP office, and submitted for federal approval. Although we noted that the budget line for additional Fringe Benefits was approved at the state and federal level, the Budget Information Worksheet references a written agreement for the use of the additional funds, which we were unable to obtain. Based on information obtained from the state's CSEPP agency, during the budget negotiation process, there was a verbal understanding about the intended use of the funds among the county CSEPP Coordinator and representatives from the state and federal level. However, there was no documentation to support this understanding, and no documentation identifying how this

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-81: The Department Of Military Affairs Should Ensure That Subrecipient Grant Expenditures Meet The Requirements Of OMB Circular A-87 (Continued)

expenditure was deemed necessary and reasonable in accordance with OMB Circular A-87. In follow-up conversations with FEMA officials, we could not obtain clear-cut information on the allowability of this expenditure, or confirm that the officials approving the county's budget had a complete understanding that the line item was intended to allow the coordinator to buy-back service credit from 1981, several years before the CSEPP grant existed.

For the 2006 grant year, the county CSEPP coordinator requested an additional \$13,300 in Fringe Benefits for reimbursement of the CSEPP Coordinator's retirement during the budget process. This request was recommended by the state program manager and approved by FEMA based on a written agreement that was not maintained in the files. The files also do not document the FEMA officials understanding of the intent of this amount, or the justification of the allowability of this charge.

The buy-back of previous service credits does not appear to be an allowable cost for the CSEPP grant because it does not meet the requirements of OMB Circular A-87, which requires federal grant expenditures to be necessary and reasonable for the administration of the grant, allocable to the grant, and properly authorized by the county's fiscal court. Also, the following items further highlight the questions regarding the allowability of the expenditure:

- The service credit purchased was from 1981, several years before the existence of the CSEPP grant.
- The county CSEPP Coordinator is the only grant-funded position in the state to receive such a reimbursement to purchase prior service time. A similar request was submitted for the FY 2007 CSSEP grant by the same coordinator and denied. The subsequent denial draws into question the allowability of the 2006 grant expense.
- The county's CSEPP Coordinator's position is funded 50% by the CSSEP grant, yet the reimbursement was for 90% of the service purchase cost.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-81: The Department Of Military Affairs Should Ensure That Subrecipient Grant Expenditures Meet The Requirements Of OMB Circular A-87 (Continued)

Attachment A of Circular A 87 C. states in part:

1. Factors affecting allowability of costs. To be allowable under Federal awards, costs must meet the following general criteria:
 - a. Be necessary and reasonable for the proper and efficient performance and administration of Federal awards.
 - b. Be allocable to Federal awards under the provisions of this Circular.
 - c. Be authorized or not prohibited under State or local laws or regulations.

Attachment B of Circular A 87 states:

8. Compensation for personal services.
 - a. General. Compensation for personnel services includes all remuneration, paid currently or accrued, for services rendered during the period of performance under Federal awards, including but not necessarily limited to wages, salaries, and fringe benefits. The costs of such compensation are allowable to the extent that they satisfy the specific requirements of this Circular, and that the total compensation for individual employees:
 - (1) Is reasonable for the services rendered and conforms to the established policy of the governmental unit consistently applied to both Federal and non Federal activities.
 - (2) Follows an appointment made in accordance with a governmental unit's laws and rules and meets merit system or other requirements required by Federal law, where applicable; . . .
 - d. Fringe Benefits.
 - (1) Fringe benefits are allowances and services provided by employers to their employees as compensation in addition to regular salaries and wages. Fringe benefits include, but are not limited to, the costs of leave, employee insurance, pensions, and unemployment benefit plans. Except as provided elsewhere in these principles, the costs of fringe benefits are allowable to the extent that the benefits are reasonable and are required by law, governmental unit employee agreement, or an established policy of the governmental unit.
 - (5) The cost of fringe benefits in the form of employer contributions or expenses for social security; employee life, health, unemployment, and worker's

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-81: The Department Of Military Affairs Should Ensure That Subrecipient Grant Expenditures Meet The Requirements Of OMB Circular A-87 (Continued)

compensation insurance (except as indicated in section 22, Insurance and indemnification); pension plan costs (see subsection e.); and other similar benefits are allowable, provided such benefits are granted under established written policies. Such benefits, whether treated as indirect costs or as direct costs, shall be allocated to Federal awards and all other activities in a manner consistent with the pattern of benefits attributable to the individuals or group(s) of employees whose salaries and wages are chargeable to such Federal awards and other activities.

Recommendation

DMA should seek reimbursement of the \$9,952 cost of the retirement purchase from the county's fiscal court, and dispense or reimburse those funds in a manner agreed upon by its federal grantor. Further, DMA should ensure that all future grant expenditures meet the requirements of OMB circular A-87 as outlined herein.

Management's Response and Corrective Action Plan

Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department and concurs with the auditor's findings. The department's internal control objective for allowable costs and cost principles is to provide reasonable assurance that federal grant awards are expended only for allowable activities and that the costs of goods and services charged to Federal grant awards are allowable and in accordance with the applicable cost principles.

CORRECTIVE ACTION PLAN:

The CSEPP Program Supervisor has forwarded this audit document to FEMA Region IV and in turn they have forwarded it to Headquarters FEMA for legal review and guidance. This questioned cost will be discussed at the Integrated Process Team (IPT) Meeting on 17 April 2008 with all the parties involved (Estill County, KyDEM, & FEMA Region IV representatives). The results of FEMA's final decision will be documented, by FEMA, in writing as to whether they will

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-81: The Department Of Military Affairs Should Ensure That Subrecipient Grant Expenditures Meet The Requirements Of OMB Circular A-87
(Continued)

Management's Response and Corrective Action Plan (Continued)

allow the expenditure to remain as a valid program and budgeted cost or to re-coop the questioned cost. All documentation of FEMA's decision will be provided to the Auditor's Office once received by the Department of Military Affairs.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-82: The Department Of Military Affairs Should Immediately Develop Corrective Action Plans For Subrecipient Audit Findings And Resolve Questioned Costs

State Agency: Department of Military Affairs

Federal Program: CFDA 97.036 - Disaster Grants-Public Assistance (Presidentially-Declared Disasters)

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: \$2,072,577

In light of nearly \$2 million of questioned costs related to Public Assistance grants (CFDA 97.036) noted in Leslie County audits for fiscal years 2004 through 2007, we reviewed the Department of Military Affairs (DMA) subrecipient monitoring of Leslie County's public assistance grants. As the pass-through entity for the Public Assistance Grant, DMA is required to ensure that required A-133 audits of subrecipients were completed, obtain the required audits, and issue a management decision for relevant audit findings. However, our review of the Leslie County projects did not determine that this monitoring has occurred. The specific monitoring deficiencies noted include:

- Failure to obtain the FY 2004 and FY 2005 single audits and issue a management decision within 6 months of the report's issuance. Although the FY 2006 and FY 2007 audits have not yet been issued, follow up of the FY 2004-2005 findings with questioned costs in excess of \$800,000 may have prevented or limited additional questioned costs identified during the FY 2006-2007 audits.
- Failure to identify questionable invoices submitted for large projects. Our review noted that the invoice for one project did not contain information sufficient to link it to the project. The contractor's invoice did not provide sufficient detail to separately identify materials, supplies, and labor charges.
- Failure to follow up on problems identified in FEMA inspection reports. The FEMA inspector noted possible problems with Leslie County's procurement procedures in the final inspection report for two projects and recommended that the state "evaluate the procurement procedures used by Leslie County for this project as set forth in paragraph 12.26(b)(11) of 44CFR." Specifically, the FEMA inspector noted the county did not:
 - Monitor the "progress of work to ensure the work was properly performed and to verify pay quantities";
 - Take measurements of the contractor's work to verify the invoiced contract;

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-82: The Department Of Military Affairs Should Immediately Develop Corrective Action Plans For Subrecipient Audit Findings And Resolve Questioned Costs (Continued)

- Obtain an itemized invoice from the contractor; or
- Advertise the project for bid, but used a contract for the materials used in the project (this bid did not include the labor or equipment invoiced for the project).

The failure to obtain the Leslie County audit reports for FY 2004 and 2005, or document attempts to obtain these audits appears to be a breakdown in the agency's internal controls over subrecipient monitoring. Our audit identified multiple exceptions related to this weakness, which has been reported in a separate finding related to DMA's subrecipient monitoring. Also, the agency's failure to scrutinize invoices and other supporting documentation prior to finalizing projects leads to additional questioned costs and increases the risk that subrecipients and contractors can expend funds that do not follow the appropriate grant requirements without detection. Further, DMA was not able to document any follow-up of Leslie County's procurement procedures as recommended in the 2005 FEMA final inspection reports. As a result of DMA's failure to review and resolve the issues noted in the county audits or FEMA inspections we are questioning \$2,072,577 of federal expenditures DMA paid to Leslie County between the 2004 and the 2007 fiscal years.

OMB Circular A-133 Subpart D-Federal Agencies and Pass-through Entities Section 400 Responsibilities states in part:

- (3) Monitor the activities of subrecipient as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
- (4) Ensure that subrecipients expending \$300,000 (\$500,000 for fiscal years ending after December 31, 2003) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
- (5) Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-82: The Department Of Military Affairs Should Immediately Develop Corrective Action Plans For Subrecipient Audit Findings And Resolve Questioned Costs (Continued)

Recommendation

We recommend that DMA immediately review the audit findings and develop a corrective action plan for the Leslie County audit findings and resolve all questioned costs. As noted in a separate finding, DMA should review and update their subrecipient monitoring procedures to ensure their compliance with OMB circular A-133. As a part of this procedure update, DMA should consider developing a system of tracking and documenting the entire process, from the determining whether a subrecipient audit is required to the resolution of audit findings and follow-up of FEMA recommendations, and clearly assigning subrecipient monitoring responsibilities to a permanent employee.

Management's Response and Corrective Action Plan

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for subrecipient monitoring is to provide reasonable assurance that Federal grant award information and compliance requirements are identified to subrecipients, subrecipient activities are monitored, subrecipient audit findings are resolved, the impact of any subrecipient noncompliance on the pass-through entity is evaluated, and subrecipients obtained required audits and take appropriate corrective action on audit findings. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

DMA concurs with the auditor's finding and has developed a corrective action plan designed to restore compliance and insure future compliance. The Federal Disaster Public Assistance Program had previously hired a position to monitor single audit reviews, but unfortunately lost the employee due to his transfer to another state agency. At that time, it became evident that the funds for this position could no longer support this salary and we were unable to backfill the position. The Kentucky Division of Emergency Management (KyDEM) is expecting a large number of their personnel to retire this year and to have large payouts for retirees. Because of these high payouts and the recent cap reductions in personnel, it will be difficult to hire or assign a position full-time to monitor the

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-82: The Department Of Military Affairs Should Immediately Develop Corrective Action Plans For Subrecipient Audit Findings And Resolve Questioned Costs (Continued)

Management's Response and Corrective Action Plan (Continued)

status of divisional internal control activities and processes during this federal fiscal year. As the budget permits and as a position becomes available, an Internal Auditor position will be included in the budget request in the Emergency Management Program Grant application for Federal FY 2009/2010 to monitor all federal grant activity for KyDEM.

The core intent of this plan is to insure that this corrective action places the right people into the right job with the right skills and the right supervision to insure that this finding does not occur again.

ACTION PLAN:

- (1) By April 15, 2008, KyDEM shall revise the current internal division policy #133-1 Subrecipient Audits / Monitoring established in 2004 to be further detailed to assure more in depth internal control procedures over Federal awards to ensure federal funds are used for authorized purposes in compliance with laws and regulations.*
- (2) By May 30, 2008, training will be conducted with all concerned KyDEM personnel on the revised policy.*
- (3) Effective July 1, 2008, each KyDEM section responsible for the dispersion of federal grant funds shall review the audits for their federal program subrecipients, when received, to comply with OMB Circular A-133 and division policy #133-1 or later approved version. A memo of record of this review shall be provided to the pre-audit section for review. The Pre-Audit Section will have a checklist to assure paperwork is completed before giving to the Assistant Director for his/her review of each subrecipient reviewed.*
- (4) Each KyDEM section responsible for the dispersion of federal grant funds shall reconcile the amount of the Federal awards reported in subrecipient audit reports and to work with the subrecipients to resolve audit findings within six months after receipt of the subrecipient audit report and ensure the subrecipient takes timely corrective action.*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-82: The Department Of Military Affairs Should Immediately Develop Corrective Action Plans For Subrecipient Audit Findings And Resolve Questioned Costs (Continued)

Management's Response and Corrective Action Plan (Continued)

(5) By July 1, 2008, the Leslie County Fiscal Court audit findings will be reviewed by KyDEM and a Management Decision issued, per OMB Circular A-133, concerning the validity of the questioned costs as well as addressing Leslie County's non-compliance with FEMA's record retention requirements which had been contractually agreed to by Leslie County at the time of their filing for federal grant assistance. Furthermore, this Management Decision will place the Leslie County Fiscal Court on probation until compliance is achieved and all current and future KyDEM grant disbursements to Leslie County will be directly dependant on their compliance with all KyDEM / FEMA audit reporting and records retention agreements.

SUMMARY:

Until a position and funds become available, revising the current procedures and adding the separation of duties in the subrecipient monitoring review in this action plan will allow for better internal control and ensure the subrecipient's reviews are followed through for completion. Issuing a Management Decision, per OMB Circular A-133, on Leslie County's audit findings will address the resolution of those questioned costs as well as help to insure Leslie County's complete compliance on their federal grant records retention and audit reporting responsibilities.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-83: The Department Of Military Affairs Should Submit Federal Reimbursement Requests Timely

State Agency: Department of Military Affairs

Federal Program: CFDA 12.401 - National Guard Military Operations and Maintenance
(O & M) Projects

Federal Agency: U.S. Department of Defense

Pass-Through Agency: Not Applicable

Compliance Area: Cash Management

Amount of Questioned Costs: \$0

The United States Fiscal and Property Office (USFPO) authorizes reimbursements to the Department of Military Affairs (DMA) for the federal portion of expenditures under National Guard Military Operations and Maintenance Projects, CFDA 12.401. Expenditures are paid through the eMARS accounting system and federal reimbursement requests, SF-270, are submitted each week. Our testing indicated that DMA is in compliance with federal cash management requirements that require reimbursement requests be made only after expenditures have been paid with state funds. However, we found significant delays in both DMA's request for reimbursement of expenditures and the USFPO's payment of the reimbursement request.

Since DMA submits the SF-270 reimbursement request weekly, ten days should be the longest between payment and reimbursement request. However, we found that for 18 of the 40 items in our test sample the reimbursement request was submitted more than 10 days after payment. For these items reimbursement was requested an average of 28 days after the expenditure had been paid and not properly included on the reimbursement request in the week that it was paid

We also noted significant delays in the receipt of the requested reimbursements from the USFPO. Once the USFPO receives the SF-270, reimbursement requests are forwarded to the appropriate Federal Program Manager (FPM) for audit, which is required prior to payment. While the USFPO has a policy to make payment within 30 days of receipt, the timeline does not begin until the audit is completed. We noted 22 instances in our sample that were more than 30 days after the submission of the SF-270.

In addition we noted six instances where the SF-270 reports had not been dated when they were signed. This makes it impossible to estimate the date of submission and could contribute to the delays in reimbursement.

These cumulative delays could create a financial hardship for DMA and impair its ability to prepay federal grant expenditures. The reimbursement process currently in place is inefficient and does not ensure timely reimbursement.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-83: The Department Of Military Affairs Should Submit Federal Reimbursement Requests Timely (Continued)

Good internal controls over cash management dictate prompt attention to all phases of the drawdown cycle. A timely reimbursement request is critical because of its impact upon cash flow. Shortening the time between federal expenditure and reimbursement allows the Commonwealth of Kentucky to maximize interest income. Further, when reimbursements closely follow expenditures, both the state and the federal grantor have a more accurate picture of actual program activity. This information aids in establishing budgets and forecasting cash flow needs.

Recommendation

DMA should review their procedures for preparing the SF-270 reports and consider improvements that will ensure that these reports include all expenditures that have occurred since the previous reimbursement request.

In addition, DMA should work with the USFPO and the Federal Program Manager to discuss the possibility of improving the audit and reimbursement process with the goal of decreasing the time needed to receive federal reimbursement.

Management's Response and Corrective Action Plan

Management's goal for the internal control process, within the Dept. of Military Affairs (DMA), is to obtain reasonable assurance that material misstatements will not occur or will be detected in a timely manner. The department's internal control objective for cash management is to provide reasonable assurance that the draw down of Federal grant cash is only for immediate needs, States comply with applicable Treasury agreement, and recipients limit payment to subrecipients to immediate cash needs. The department's current internal control environment, effected by executive management, establishes management's full support of ethical, efficient, and effective internal control activities and sets a positive tone for correction of identified deficiencies.

Based on the auditor's findings, DMA management has conducted an analysis of the overall risk environment currently facing the department from this finding and concurs with the auditor's finding.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DMA-83: The Department Of Military Affairs Should Submit Federal Reimbursement Requests Timely (Continued)

Management's Response and Corrective Action Plan (Continued)

CORRECTIVE ACTION PLAN:

State Manual Billing Invoice Delays: DMA- Office of Management and Administration (OMA) will re-issue and enforce departmental fiscal policy statement 'Internal Control for Cash Management: Departmental Fiscal Policy & Procedures for Processing eMARS Grant / Cost Accounting Billings. This policy will supercede the previous policy issued in 1999 with all changes. This revised and re-issued policy will require all DMA grant fiscal administrator personnel who process manual billing invoice documents per federal grant instruction (such as the SF-270) to fully complete the manual preparation of their billing invoice within 5 calendar days (or sooner if possible) after the eMARS automated billing occurs and the revenue becomes due the state and to expedite, by the fastest means available, the transmittal of this manual billing invoice to the federal grantor by close of business on that day. This '5 day or sooner' rule will also apply to initiating and inputting draw down reimbursement requirements into any federal automated draw down system, when allowed, for EFT payment receipt.

Federal Payment Delays: DMA-OMA will coordinate with the federal grantor of the DoD Cooperative Agreements to deliver the manual billing invoice (i.e. SF-270) documents directly to the federal contracting official / grants management officer with the objective being to obtain faster auditing and review and payment within the 30 day window of the federal Prompt Payment Act.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DWI-84: The Department For Workforce Investment Should Ensure Activity Does Not Affect Closed Grants

State Agency: Department for Workforce Investment

Federal Program: CFDA 84.048 - Vocational Education-Basic Grants to States

Federal Agency: U.S. Department of Education

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Costs: \$2,649

During our testing of the Consolidated Annual Accountability Report (CAR) for the reporting period of 7/1/2004 to 9/30/2006, we noted the Total State Leadership amount in the "Federal share of outlays and unliquidated obligations" column, \$1,692,838 did not agree to the eMARS amount of \$1,685,366. The difference of \$7,472 relates to:

- A negative cash expenditure of \$1,003 was charged against the grant after it closed. This related to document Journal Voucher Entry (JVE) 721 0700006419, which was created by CHFS personnel and overridden by the Finance Administration Cabinet (FAC). DWI was not aware of this document until after we inquired about the differences between the expenditures in the grant screen used for the CAR report and the grant screen available February 20, 2008 in eMARS. Since the grant was closed, no additional expenditures should have been posted to the grant.
- Commodity Based Purchase Request (PRC) 531 070000155144 in the amount of \$2,649. This amount was an encumbrance liquidation. The encumbrance is included in the cash expenditure amount on the grant screen used for preparing the report for the 05 project. Basically, the amount was obligated at the end of the grant, drawn down by DWI, and reported on the CAR. However, the encumbrance was never actually spent so the PRC was done to liquidate the encumbrance. When it was actually paid and liquidated after Jan 1, it was paid against the 06 project. The result was that the \$2,649 was applied to the 05 project (although subsequently liquidated after Jan 1), but will also show as a payment against the 06 project. This amount should be repaid to the US Department of Education and the report amended.
- The remaining difference is unexplained.

An agency other than DWI created a document and FAC overrode the document. DWI did not have procedures in place to detect documents affecting closed grants.

Expenditures were charged against a closed grant, which made the current grant screen different from the grant screen used for the final report.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DWI-84: The Department For Workforce Investment Should Ensure Activity Does Not Affect Closed Grants (Continued)

We do not know the reason for the unexplained differences on the grant screen.

A document being created by one agency, without the other agency's knowledge can lead to errors in the accounting system. The JV2E document (recorded January 12, 2007) was not processed properly and this went undetected by DWI and CHFS for more than a year.

The CAR report is not accurate and the state owes the Federal government \$2,649.

We cannot verify the amount reported to the Federal government was correct for the Total State Leadership amount in the "Federal share of outlays and unliquidated obligations" column.

Good internal controls dictate that an agency should not create a document impacting another agency's grant without that agency's knowledge.

Also, good internal control dictate that amounts submitted to the Federal government be as accurate as possible. If the grant screen amount can be changed after the grant is closed, the grant screens are not reliable and the report should be completed using another information source.

Recommendation

We recommend DWI:

- Review current procedures to ensure activity does not occur for closed grants now or in the future.
- Meet with FAC regarding the ability of other agencies to impact expenditures for DWI's grants.
- Contact the US Department of Education to discuss repaying the amount and amend the final CAR report for this grant.
- Investigate the reason behind the unexplained differences.

Management's Response and Corrective Action Plan

We agree that activity after a project is closed affects the accuracy of our federal reports. eMARS, as with any new accounting system, obviously has some issues that we need to be aware as we learn of them as is the case with this finding.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-DWI-84: The Department For Workforce Investment Should Ensure Activity Does Not Affect Closed Grants (Continued)

Management's Response and Corrective Action Plan (Continued)

Since apparent activity can happen on a closed project, even by outside agencies beyond our control, we will be watching for such transactions and will be able to correct them as will be done with the journal voucher (JV) noted in the finding.

Also in preparing final reports, encumbrances on the grant screen will need to be analyzed to see how it affects the final expenditure balance and may need to be deducted from the final expenditure amount to calculate a correct ending expenditure balance.

We will request the USDOE, Office of Vocational and Adult Education (OVAE) to ask their contractor to open the CAR website so that we can make corrections. We will also be repaying the amount that needs to be returned.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-EPPC-85: The Division Of Forestry Needs To Communicate Federal Award Information To All Subrecipients

State Agency: Environmental and Public Protection Cabinet
Federal Program: CFDA 10.664 - Cooperative Forestry Assistance
Federal Agency: U.S. Department of Agriculture
Pass-Through Agency: Not Applicable
Compliance Area: Subrecipient Monitoring
Amount of Questioned Costs: \$0

The Division of Forestry (DOF) needs to directly communicate award identification information and related compliance requirements to all subrecipients. The auditor reviewed the 13 CPG Program projects active during FY 2007. Of these, 12 adequately presented all federal award and compliance requirements. The agreement with the KY Association of Consulting Foresters, however, contained no reference to the federal award or to the compliance requirements.

The failure to directly and clearly communicate the Federal award identification information and applicable compliance requirements constitutes non-compliance.

Subpart D of the OMB Circular A-133 states the following:

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:
 - (1) Identify Federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is Research and Development (R&D), and name of Federal agency. When some of this information is not available, the pass-through entity shall provide the best information available to describe the Federal award.

Recommendation

We recommend that DOF take steps to clearly and directly communicate the Federal award identification information and related compliance requirements to

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-EPPC-85: The Division Of Forestry Needs To Communicate Federal Award Information To All Subrecipients (Continued)

Recommendation (Continued)

all subrecipients. The agency could consider adding or modifying a section of the MOA so that it expressly communicates all of the required information to subrecipients. For example:

CFDA Title: Cooperative Forestry Program

CFDA Number: 10.664

Award Name and Number: (state grant name and number here)

Name of Federal Awarding Agency: United States Department of Agriculture

Applicable Compliance Requirements: (state applicable compliance requirements here, including Circular A-133)

We also recommend that DOF consider adding or modifying current language of the contract so that the designated official of the subrecipient signs the Master Agreement (MOA) acknowledging that “they were informed of, understand, and agree to comply with applicable compliance requirements”.

Management Response and Corrective Action Plan

The omission of the information on one of the thirteen contracts was an error. DOF staff have been notified and instructed regarding information requirements. The contract template modifications recommended by the Auditor’s Office will be given to EPPC’s Office of Legal Services for consideration.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-EPPC-86: The Abandoned Mine Lands (AML) Should Make Timely Payments To Vendors

State Agency: Environmental and Public Protection Cabinet

Federal Program: CFDA 15.252 - Abandoned Mine Land Reclamation (AMLR) Program

Federal Agency: U.S. Department of Interior

Pass-Through Agency: Not Applicable

Compliance Area: Activities Allowed or Unallowed, Allowable Costs/Cost Principles

Amount of Questioned Costs: \$0

During FY 2007, AML did not make timely payments to vendors. Forty expenditures were selected and tested for adequate support and timely payment. The results of our tests noted nine payments totaling \$601,011 was paid more than 30 days after receipt of an invoice from the vendor, a 20% error rate.

All of the late payments were made in the first two months of the fiscal year. It appears that the transition from Management Administrative Reporting System (MARS) to eMARS contributed to the problem.

Kentucky Revised Statute (KRS) 45.451 through KRS 45.458 and Finance and Administration policy BO 120-05-00 address prompt payment to vendors. The policy can be summarized, as "all bills shall be paid within 30 working days of receipt of goods and/or services, except when the purchasing agency has transmitted a rejection notice to the vendor."

In addition, the purchasing agency is responsible for a 1% penalty when payment is not made within 30 days.

Recommendation

We recommend that payments be made in a timely manner. Controls should be developed and implemented to ensure payments are made in a reasonable time frame in compliance with legal statutes. The agency should review the statutes and policy noted above to ensure full compliance. The agency should take steps to ensure that the people involved in processing and approving payments read and understand the relevant laws and policies.

Management Response and Corrective Action Plan

The late payments occurred because of the conversion from the MARS accounting and financial tracking system to the eMARS system. Contracts that were entered

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-EPPC-86: The Abandoned Mine Lands Should Make Timely Payments To Vendors (Continued)

Management Response and Corrective Action Plan (Continued)

into MARS did not convert properly into the eMARS system. AML could not make payments against these contracts until the conversions were corrected. Consequently, several payments exceeded the 30-day window for payment. Since then, AML has been able to make all payments within the 30-day window. No corrective action plan is necessary.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-EPPC-87: The Abandoned Mine Lands Subrecipients Required To Submit A-133 Reports Should Be Tracked

State Agency: Environmental and Public Protection Cabinet

Federal Program: CFDA 15.252 - Abandoned Mine Land Reclamation (AMLR) Program

Federal Agency: U.S. Department of Interior

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: \$0

We examined EPPC's system for tracking AML subrecipients required to have an A-133 audit. Four subrecipients received over \$500,000 in federal funding from EPPC alone. Only two audit reports were received, but these were not submitted within nine months of the entity's fiscal year end. Both audit reports were reviewed and accepted within six months of receipt by EPPC.

It should be noted that AML has adequate procedures in place for all other aspects of the Subrecipient Monitoring portion of the A-133 Compliance Requirement. No exceptions were found during testing of this compliance requirement except for those relating to subrecipient audit reviews.

Failure to obtain required audit reports and review the audit reports could result in a reduction of Federal funds.

Section 400(d) of the OMB Circular No. A-133 states the following:

- (d) Pass-through entity responsibilities. A pass-through entity shall perform the following for the Federal awards it makes:
 - (4) Ensure that subrecipients expending \$500,000 or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.

Recommendation

We recommend EPPC implement a tracking system/log to locate all subrecipients receiving at least \$500,000 in funding from EPPC as a whole during one fiscal year. They should then send a letter to these subrecipients stating that a single audit may be needed. It is the APA's experience that for many local governments requiring a single audit, a program will be considered a major program tested at the subrecipient level if the local government received at least \$500,000 in funds.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

**FINDING 07-EPPC-87: The Abandoned Mine Lands Subrecipients Required To
Submit A-133 Reports Should Be Tracked (Continued)**

Recommendation (Continued)

We also recommend these letters be generated shortly after fiscal year end and be included in the audit tracking system. The A-133 audits are required to be submitted nine months after the end of the subrecipients' fiscal year. The fiscal year end is usually June 30. When a needed A-133 audit on a subrecipient has not been received by March 1, EPPC should conduct follow-up by mail and by phone. These steps should greatly increase the likelihood of compliance by March 31 each year.

Management's Response and Corrective Action Plan

Subrecipient agreements that are signed by both parties specify the requirement for an audit. The Division of Fiscal Management has devised a report that totals the amount by vendor for both total contract amount and payments (since staff-generated logs lend themselves to errors). A letter will be sent to any vendor that has reached the \$500,000 threshold near June 30. When an anticipated A-133 subrecipient audit has not been received by March 1, EPPC staff will conduct follow-up by mail and/or phone.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-FAC-88: The Finance And Administration Cabinet Should Improve Controls Related To The Cash Management Interest Liability Calculation To Ensure It Is Accurate

State Agency: Finance and Administration Cabinet

Federal Program: All Major Federal Programs

Federal Agency: U.S. Department of Agriculture, U.S. Department of Defense, U.S. Department of Education, U.S. Department of Health and Human Services, U.S. Department of Homeland Security, U.S. Department of the Interior, U.S. Department of Labor, U.S. Department of Transportation, U.S. Environmental Protection Agency

Pass-Through Agency: Not Applicable

Compliance Area: Cash Management

Amount of Questioned Costs: \$0

We tested the data used on the Cash Management Information Act (CMIA) Interest Liability worksheet to verify the accuracy of the interest liability calculation. Specifically, we verified 18 bank deposit dates in eMARS, 3 bank deposit dates from bank reports provided by Treasury that were not available in eMARS, and 2 dates due from the federal government for 21 of the 185 CR documents listed on the CMIA Interest Liability worksheet.

From discussion with FAC, we determined that 36 bank deposit dates, for the 185 Cash Receipt (CR) documents listed on the CMIA Interest Liability worksheet, were not entered in eMARS, and were provided by Treasury to FAC. We asked Treasury to provide us with the bank reports for these CR documents for verification of the dates used in the worksheet. Three of the 36 dates noted on the CMIA Interest Liability worksheet, as provided by Treasury, were incorrect, when compared to the bank reports.

The draw data sheets and CR document approval information was provided by Treasury for 2 of the 3 CR documents referred to above. The date provided as the date due from the federal government on the CMIA Interest Liability worksheet for those two documents was the last action date on the CR documents in eMARS, not the draw dates indicated on the draw data sheets. FAC requests agencies provide information for the CMIA Interest Liability worksheet via certification letters, but the instructions for the “date due from federal government,” do not clearly request the draw date.

Our testing concluded the following:

- The dates used to calculate the interest liability for 3 CR documents were incorrect; therefore, there is potential that other dates used in the worksheet are incorrect. Thus, the interest liability calculation for FY07 is incorrect.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-FAC-88: The Finance And Administration Cabinet Should Improve Controls Related To The Cash Management Interest Liability Calculation To Ensure It Is Accurate (Continued)

- FAC was not aware of the errors on the CMIA Interest Liability worksheet until the auditor informed them of the errors. FAC does not perform procedures to verify the information provided by other agencies on the CMIA Interest Liability worksheet.

Since FAC did not verify the dates provided by other agencies, which were used in the interest liability calculation, and the dates tested were incorrect, the interest liability calculation for FY07 is incorrect.

If the information used in calculating the interest liability is not verified by FAC, and clear instructions are not provided to the agencies to request information to be used in the calculation, then the risk that the calculation is incorrect increases due to agency reporting error either through communication to FAC or in eMARS reporting.

CFR title 31, section 205.14, subsection c, regulates, "States must adhere to Federal Program Agency disbursement schedules when requesting funds. States must time their fund drawdowns so that it does not create Federal interest liability. The drawdown request must allow the Federal Program Agency sufficient time to meet its disbursement schedule."

Good internal controls dictate to decrease the risk of an incorrect interest liability calculation, the instructions for the compilation of the supporting worksheet must be adequate, specific and adhered to and the information used in the calculation should be verified.

Recommendation

We recommend the interest liability due from the federal government for FY07 be recalculated by FAC and resubmitted to the federal government.

We also recommend, in preparing future CMIA reports, FAC:

- Develop written instructions on how the CMIA Interest Liability worksheet is compiled;
- Clarify instructions in the certification letters to specify exact information requested from agencies;
- Create and implement procedures to review and verify the information received by other agencies to be used in the interest liability calculations; and
- Check the interest liability calculation formulas for accuracy.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-FAC-88: The Finance And Administration Cabinet Should Improve Controls Related To The Cash Management Interest Liability Calculation To Ensure It Is Accurate (Continued)

Management's Response and Corrective Action Plan

Recommendation 1: We recommend the interest liability due from the federal government for FY07 be recalculated by FAC and resubmitted to the federal government.

Response: Liability for those interest calculations using an incorrect Bank Deposit Date will be submitted as prior year adjustments for the 2008 CMIA Annual Report.

Recommendation 2: Develop written instructions on how the CMIA Interest Liability worksheet is compiled.

Response: Written instructions are used by those persons in FAC responsible for completing the Annual Report. Written instructions have been used for a number of years. Agencies are given written instructions only for the portion of the Annual Report that requires their response.

Recommendation 3: Clarify instructions in the certification letters to specify exact information requested from agencies.

Response: Written instructions are e-mailed to agencies having CMIA reportable activity. The instructions include only items needed for completion by the agencies. The only item requested from agencies for Interest Liability worksheets is the date that funds were due from the federal government, which is understood by the agency personnel completing the worksheet.

Confusion exists with APA over the "date due" from the federal government on the CMIA Interest Liability worksheet and the "draw date" from the draw data sheets, as noted in Condition, paragraph 3. The "date due" is the date that funds should have been drawn from the federal government and is only available from the agencies making the draw. It is each agency's responsibility to time the drawdown of funds so that funds are deposited on the date due. There were some timing issues during fiscal year 2007 that caused funds to not be deposited on a timely basis, creating a federal interest liability. This issue has been addressed with the agencies in question, with the assurance that this should not be an issue in fiscal year 2008.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-FAC-88: The Finance And Administration Cabinet Should Improve Controls Related To The Cash Management Interest Liability Calculation To Ensure It Is Accurate (Continued)

Management's Response and Corrective Action Plan (Continued)

The "draw date" is the actual date the funds are posted to the Commonwealth's financial institution, Farmers Bank and Capital Trust Company. The "draw date" is not requested from the agencies, as this information is provided from a query prepared by the State Report Administrator, and is noted on the Interest Liability worksheet as the "Bank Deposit Date". The "Bank Deposit Date" information is entered into eMARS through the Deposit Reconciliation Table (DPREC) by the State Treasurer's Office based on draw data sheets received from Farmers Bank. There were 59 total instances where State Treasurer's Office did not enter the "Bank Deposit Date" into the Deposit Reconciliation Table. A spreadsheet was e-mailed to the appropriate personnel in the State Treasurer's Office requesting that the files be reviewed and a date provided when funds were deposited into Farmers Bank. APA has noted three instances (out of the 59) where an incorrect date was used by the State Treasurer's Office. FAC relied on the information provided by the State Treasurer's Office to complete the Interest Liability worksheet and had no reason to question the responses given. Agencies are not responsible to provide FAC with the date funds are withdrawn.

Recommendation 4: Create and implement procedures to review and verify the information received by other agencies to be used in the interest liability calculations.

Response: FAC e-mails each agency having CMIA reportable activity a certification letter. The agency representative signs and certifies that, to the best of their knowledge, the information provided for the CMIA interest calculation is complete and accurate. Based on this certification, FAC reviews the information and compiles schedules for the CMIA Annual Report.

Recommendation 5: Check the interest liability calculation formulas for accuracy.

Response: FAC staff currently reviews the interest liability calculation schedules for accuracy.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-FAC-88: The Finance And Administration Cabinet Should Improve Controls Related To The Cash Management Interest Liability Calculation To Ensure It Is Accurate (Continued)

Auditor's Reply

To calculate an accurate timing difference for the interest liability, the actual draw date and the date the funds were deposited in the bank should be used. The date on the CR document in eMARS, which appears to be provided by the agency for the date due to the federal government, is not always the same as the draw date, or the date the funds should have been drawn. The bank deposit date in eMARS is not always the draw date. Therefore, the current method of compiling dates used is not accurate for calculating a timing difference for the interest liability.

FAC informed the auditors that the federal government requested the bank deposit dates and the dates due from the federal government for the documents listed on the CMIA Interest Liability worksheet, after this finding was issued and addressed by FAC. In response to the federal government's request, FAC requested the dates from the state agencies. One state agency provided different dates than they provided for FAC's previous request. Since some of the dates provided by the State Treasury were incorrect and one state agency provided different dates in a second inquiry, FAC requested that the federal government deny the CMIA interest liability claim for FY 07.

Though FAC depends on various agencies to provide dates used to calculate the interest liability, it is FAC's responsibility to ensure that the interest liability calculation is accurate.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-KOHS-89: The Kentucky Office Of Homeland Security Should Improve Internal Controls Over The Preparation Of Its SF-269 Financial Status Report

State Agency: Kentucky Office of Homeland Security

Federal Program: CFDA 97.004 - State Domestic Preparedness Equipment Support Program

CFDA 97.067 - Homeland Security Grant Program

CFDA 97.008 - Urban Areas Security Initiative

Federal Agency: U.S. Department of Homeland Security

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Costs: \$0

During the FY 07 audit of the Kentucky Office of Homeland Security (KOHS) we reviewed the SF-269 reports submitted to the Federal government for various KOHS grants. We found that KOHS misstated the amount of expenditures reported during the year by incorrectly reporting expenditures based upon the date the funds were drawn down from the federal government instead of reporting them based upon the date they were expended.

Apparently the SF-269 reports have been prepared in the same manner for several years and the misreporting likely results from either misunderstanding of or not reviewing the SF-269 instructions prior to the report preparation.

The expenditures reported to the Federal government on lines 10a (total outlays), and 10c (Federal share of outlays) of the SF-269 were misstated by the amounts listed below.

GRANT	REPORTING PERIOD	SF-269 OUTLAYS	eMARS EXPENDITURES	DIFFERENCE
UASI	7/1/06-9/30/06	1,842,717	1,960,625	(117,907)
UASI	10/1/06-12/31/06	2,110,584	1,992,677	117,907
HOMELAND SECURITY CLUSTER	7/1/06-9/30/06	5,190,981	4,983,341	207,640
HOMELAND SECURITY CLUSTER	10/1/06-12/31/06	3,885,750	3,447,976	437,774
HOMELAND SECURITY CLUSTER	1/1/07-3/31/07	5,217,904	5,226,654	(8,750)
HOMELAND SECURITY CLUSTER	4/1/07-6/30/07	6,782,952	6,877,881	(94,929)

These misstatements could have unintended adverse consequences such as erroneous decisions or inaccurate reporting by the users of the SF-269.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-KOHS-89: The Kentucky Office of Homeland Security Should Improve Internal Controls Over The Preparation Of Its SF-269 Financial Status Report (Continued)

For reports prepared on the cash basis of accounting, the SF-269a report instructions state that “outlays are the sum of actual cash disbursements for direct costs for goods and services, the amount of indirect expense charged, the value of in-kind contributions applied, and the amount of cash advances and payments made to subrecipients.”

Recommendation

We recommend that KOHS prepare the SF-269 on a cash basis of accounting, which includes reporting expenditures when paid.

Management’s Response and Corrective Action Plan

The Kentucky Office of Homeland Security prepares the quarterly SF-269 reports based on U. S. Department of Homeland Security guidelines. The eMARS system generates a weekly report that we base our SF-269 report on. As it is a weekly report and the quarters do not always end on a Friday we do not always receive an accurate expense report for the full quarter. However, those expenses are reported on the next quarter’s SF-269 report.

Auditor’s Reply

The SF-269 is a cash basis report, and should include all expenditures made during the reporting period. The KOHS response indicates it uses a weekly eMARS report to prepare the report, and the differences are timing differences since the end of the quarter may not coincide with the end of the week. However, eMARS users have the capability of generating custom reports, and KOHS should utilize that functionality to extract expenditures for the report. Given the size of potential reimbursements, these timing differences could materially misstate the quarterly reports submitted to the federal government. We recommend that KOHS work with Finance to modify their reporting procedures to extract the expenditures from eMARS so that the SF-269 is accurate when submitted.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-90: The Kentucky Transportation Cabinet Should Ensure Federal Reports Are Accurately Prepared And Completely Supported

State Agency: Kentucky Transportation Cabinet

Federal Program: CFDA 20.205 - Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Reporting

Amount of Questioned Costs: \$0

The Kentucky Transportation Cabinet (KYTC) is responsible for submitting an Office Of Real Estate Services Annual Program Statistics Report to the Federal Highway Administration (FHWA) for each federal fiscal year (FFY). KYTC maintains supporting documentation for right of way acquisition, condemnation, and relocation payments in order to submit accurate totals per type of relocation to the FHWA. During our review of the Statistical Report for FFY 2007, we noted several inconsistencies. The following discrepancies are repeat findings from FY05 and FY06:

- Data appearing in the eMARS InfoAdvantage reports were not included on the agency's monthly reconciliations;
- Items were left off or added twice;
- Items paid out of an incorrect activity and or reporting codes;
- Information included in reports that did not belong.

The report inaccurately underreported the amounts falling under the acquisition and condemnation categories from KYTC's internal documentation by a combined \$1,209,085 and from eMARS by a combined \$158,166.

In FY07 a new issue came to our attention regarding the relocation amounts. KYTC could not provide us with the supporting documentation for the relocation payments, and, therefore, we were unable to determine whether relocation amounts reported to the FHWA were accurate.

The "Office of Real Estate Services Annual Program Statistics Report" is not being properly reviewed. KYTC Division of Right of Way and Utilities indicated in its response to last year's finding that it had improved its record keeping procedures by recording reporting categories in eMARS for acquisition and relocation expenditures. The division also said it improved their record keeping by maintaining monthly spreadsheets with information related to the statistical report. However, management is not performing an in-depth review of these spreadsheets or this report.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-90: The Kentucky Transportation Cabinet Should Ensure Federal Reports Are Accurately Prepared And Completely Supported (Continued)

The management response in FY06 stated that the implementation of eMARS caused some difficulty in performing the needed queries. However, it also stated that they were able to pull and query the needed information after they reviewed the eMARS system. Corrective action was to perform a closer review of the reporting categories, review the report every month, and perform a closer review of the end of the month transaction to ensure they are reported accurately. We did not see any evidence that this in-depth review was performed.

KYTC indicated the inability to provide us with a complete listing of relocation payments is due to employee turnover. Only half of the transaction log for FFY 2007 was available for review. According to KYTC personnel, the computer file for the relocation log was no longer available after the employee that maintained these records transferred to another position. KYTC personnel are recreating the relocation log file, but the complete listing of FFY 2007 relocation transactions was not available for reconciliation.

Without proper supporting documentation maintained there is a risk that reports to the FHWA may not be reliable or accurate.

Without proper management oversight there is a risk of inaccurate data being reported.

The inability for KYTC to provide its complete log for tracking relocation payments makes it impossible to verify the amounts submitted to the FHWA.

According to 49 CFR 24 Appendix B - Statistical Report Form, "Report Coverage - This report covers all relocation and real property acquisition activities under a Federal or federally assisted project or program subject to the provisions of the Uniform Act." All information and amounts contained in the FHWA Statistics Report should be accurate and trace to supporting documentation on file at the agency.

Good internal controls dictate that supporting documentation be maintained in order to provide accurate and complete data for reporting to the FHWA. KYTC is responsible for providing a listing of relocation payments it entered into eMARS and subsequently reported to the FHWA.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-90: The Kentucky Transportation Cabinet Should Ensure Federal Reports Are Accurately Prepared And Completely Supported (Continued)

Recommendation

We recommend:

- The KYTC Division of Right of Way and Utilities improve the procedures for tracking and compiling information for the Statistical Report.
- The KYTC Division of Right of Way and Utilities immediately implement procedures to improve document retention, especially addressing transition of records in the event of employee turnover
- The KYTC Division of Right of Way and Utilities provide more management oversight on the preparation and submission of the Statistical Report to prevent inaccurate data from being reported to the FHWA.

Management's Response and Corrective Action Plan

KYTC takes these audits seriously and has been responsive each year to findings. As a result of the FY05 and FY06 audits and recommendations, the Division of Right of Way & Utilities developed a new spreadsheet which replaced the prior transaction log, to assist in tracking acquisition, condemnation, and relocation payments for the Federal Annual Program Statistics Report that is submitted to FHWA. This relocation spreadsheet was finished and put into use April 2007 and therefore would not include all the information typically required for audit purposes for the current FY being audited. However, the information needed to complete the federal report is and has been maintained in KYTC files, along with other supporting documents.

The Division of Right of Way maintains monthly spreadsheets showing the amount of monies spent on ROW acquisitions, condemnations, and relocation payments for all federal projects. The spreadsheets are then balanced against an eMARS query for accuracy at the end of each month. This spreadsheet along with the eMARS data is made part of the federal report at the end of the federal fiscal year. Payments that show up twice are due to checks being redeposited and reissued due to time delays or due to a court proceeding which require a payment being made to different or additional parties. In the past demolition costs were made part of the federal report but those cost are now paid out through contracts and are not required for the report but were provided in the spreadsheets at the request of KY FHWA for their review. Furthermore, there are times when KYTC will receive refunds on overpayments for condemnation cases as a result of

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-90: The Kentucky Transportation Cabinet Should Ensure Federal Reports Are Accurately Prepared And Completely Supported (Continued)

Management's Response and Corrective Action Plan (Continued)

settlements or jury awards in the Commonwealth's favor. Refunds that are due the Commonwealth on cases that were prior to eMARS are deposited but not made part of KYTC's monthly spreadsheet and show up in the eMARS queries as credits. These credits may not be based on the current FY and do not have an eMARS document ID to reference. The spreadsheet the Division uses is being revised to include deposits so they will now reconcile to eMARS.

Spreadsheets have been integrated into Project Wise and are backed up by COT daily to ensure daily maintenance of spreadsheets and that employee turnover will have little or no impact on the maintenance of these records. In FY 06 the Division initiated a cross training program to also ensure that more than one employee in each area has knowledge of the spreadsheet and information which also helps to offset any employee turnover.

Auditor's Reply

The discrepancies noted in the finding are related to the agency's lack of reconciliations. The intent of the finding is for KYTC to improve its ability to ensure reports are complete and accurate prior to their submission to federal agencies.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-91: The Kentucky Transportation Cabinet Should Ensure Independence With Right Of Way Employees, And Should Adhere To Established Procedures Regarding The Approval Process Of Right Of Way For State Employees

State Agency: Kentucky Transportation Cabinet

Federal Program: CFDA 20.205 - Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Activities Allowed or Unallowed, Allowable Costs/Cost Principles

Amount of Questioned Costs: \$0

In FY2007, a review of the Kentucky Transportation Cabinet (KYTC) Right of Way (ROW) Acquisitions was performed. During this review we noted that KYTC acquired property from a KYTC Division of Right of Way employee without following proper approval procedures. The files did contain a memorandum from the District Supervisor to the Division Director; however, no other required approvals were obtained.

During the review it was also noted that the same KYTC ROW employee was also identified as the acquisition agent that negotiated other parcels of property that were sold to KYTC for the same highway project. This employee also determined the sales range per acre for parcels to be acquired by minor acquisition reviews, which determined the pricing for property to be acquired for the project when an appraisal was not required. Documentation shows that for this project, the sales range for residential increased from \$10,000 per acre to \$12,000 per acre. Therefore, it appears that the value of the parcel of land sold to the KYTC by this employee was determined by a sales range set by the same employee.

Although KYTC policies do permit acquisition of property from state employees, there is an extensive review and approval procedure that was not followed in this case. Because the employee works for the agency and was involved in key elements of the project, it leads to an appearance of impropriety. Conflicts of interest exist when an employee negotiates property for the same project in which they are selling their own property. The value of the property comes into question when the acquisition agent is not independent.

We acknowledge that the lack of approvals could be a result of management oversight, but failure to obtain proper approvals prior to acquisition of Right of Way appears to be noncompliant with internal policies and state statute.

Per KRS 45A.045 (9), "Except as provided in KRS Chapters 175, 176, 177, and 180, and subject to the provisions of this code, the Finance and Administration Cabinet shall purchase or otherwise acquire all real property determined to be needed for state use,

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-91: The Kentucky Transportation Cabinet Should Ensure Independence With Right Of Way Employees, And Should Adhere To Established Procedures Regarding The Approval Process Of Right Of Way For State Employees (Continued)

upon approval of the secretary of the Finance and Administration Cabinet as to the determination of need and as to the action of purchase or other acquisition. The amount paid for this real property shall not exceed the appraised value as determined by the cabinet or the Transportation Cabinet (for such requirements of that cabinet), or the value set by eminent domain procedure. Subject to the provisions of this code, real property or any interest therein may be purchased, leased, or otherwise acquired from any officer or employee of any agency of the state upon a finding by the Finance and Administration Cabinet, based upon a written application by the head of the agency requesting the purchase, and approved by the secretary of the Finance and Administration Cabinet and the Governor, that the employee has not either himself or herself, or through any other person, influenced or attempted to influence either the agency requesting the acquisition of the property or the Finance and Administration Cabinet in connection with such acquisition. Whenever such an acquisition is consummated, the request and finding shall be recorded and kept by the Secretary of State along with the other documents recorded pursuant to the provisions of KRS Chapter 56.”

According to the Division of Right of Way Guidance Manual, ROW-806-4 *Conveyance Involving a State Employee*, “When a state employee conveys right-of-way, the payment request submitted to the Central Office is to be accompanied by a certification from the district right-of-way supervisor. The certification is to state that the state employee, because of his or her position, reached the agreement without any influence. The certification is to include the state employee’s:

- Name
- Social Security Number
- Agency of Employment

A request is made for approval from the Finance and Administration Cabinet Secretary and the Governor upon receipt of the following in the Central Office:

- Payment request
- Certification.”

According to 49 CFR 24 Subpart B - §24.102 (n) *Conflict of interest*. (1) The appraiser, review appraiser or person performing the waiver valuation shall not have any interest, direct or indirect, in the real property being valued for the Agency.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-91: The Kentucky Transportation Cabinet Should Ensure Independence With Right Of Way Employees, And Should Adhere To Established Procedures Regarding The Approval Process Of Right Of Way For State Employees (Continued)

Recommendation

We recommend that the KYTC Division of Right of Way provide the appropriate oversight on acquisition approvals for state employees and obtain approvals prior to acquisition. We also recommend that KYTC restrict employees in the Division of Right of Way from being assigned to projects involving property in which they or family members own. This policy should be included in a conflict of interest statement signed by all KYTC Division of Right of Way employees.

Due to the concerns noted regarding a possible conflict of interest, we are referring this finding to the KYTC Office of Inspector General.

Management's Response and Corrective Action Plan

The ROW acquisition agent for this transaction was assigned as negotiator for the subject project in the summer of 2005, at which time she was not identified by the district design staff as a parcel owner being affected by the proposed highway project. As an experienced ROW agent, this employee was assigned to compile the market data and complete a "range of values," which was approved by the ROW supervisor. This practice is in accordance with the ROW policy entitled ROW-702, in the 2001 ROW guidance manual. The ROW acquisition agent allocated \$12,000 per acre for home sites in the "range of values" memo, which was actually lower than the \$14,000 per acre allocated for Parcel No. 001, the \$14,200 per acre allocated for Parcel No. 009, and the \$15,715 per acre allocated for Parcel No. 008--all by the assigned appraiser for subject project.

At the beginning of subject project, Parcel No. 005 was identified as an "Unknown Owner." Several members of the District ROW staff spent a considerable amount of time trying to locate the rightful owner of Parcel No. 005. ROW staff researched the records at the Edmonson County PVA office, the Edmonson County Court Clerk's office, and the Edmonson County Sheriff's office, all to no avail. As a final measure, all parcel owners of the subject project were also asked if they knew who owned Parcel No. 005; none of the owners knew nor claimed ownership. On June 29th, 2006, the ROW Supervisor recommended that Parcel No. 005 be submitted for condemnation and a ROW agent submitted the parcel batch to central office.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-91: The Kentucky Transportation Cabinet Should Ensure Independence With Right Of Way Employees, And Should Adhere To Established Procedures Regarding The Approval Process Of Right Of Way For State Employees (Continued)

Management's Response and Corrective Action Plan (Continued)

In December 2006, the acquisition agent informed the district supervisor that in 1990 when she and her husband purchased their property, which adjoins Parcel No. 005, the owner at the time was unsure about the property or boundary lines and their driveway actually encroaches on Parcel No. 005. The acquisition agent informed the district supervisor that she and her husband were going to pursue ownership of Parcel No. 005 through adverse possession. Mr. Devine discussed this matter with the district highway attorney and he stated that if she and her husband provided KYTC with a deed and clear title to the property, they would be the rightful owner and good faith negotiations should commence.

In mid-January 2007, the district supervisor was provided a deed showing the appropriate property owners were the Cabinet employee and her husband. The district supervisor then notified central office acquisition branch manager and discussed the situation whereby the cabinet employee and her husband were now parcel owners on the subject project. In order to avoid a conflict of interest, it was decided that negotiations for parcel 005 should be handled by the Elizabethtown District Highway D4 office. The district supervisor contacted the D4 ROW supervisor about the matter and he recommended that one of D4's agent handle the negotiations. The district supervisor agreed. The D4 agent then came to the D3 office and he was provided a set of plans and a title report. The district supervisor then gave D4's agent the option to complete his own Range of Values or use the values already relied upon. He indicated that he felt comfortable using the existing values and there is a memo in the file to this affect. D4 agent then completed the MAR calculation on January 25th, 2007 and the district supervisor approved it on the same date. The MAR calculation is in the file. The D4 agent began negotiations with the cabinet employee and her husband on January 26th, 2007 and a settlement was reached on January 29th, 2007.

We realize this real estate transaction is being reviewed by several parties. D4 personnel handled the negotiations to avoid a potential conflict of interest and a memo was submitted informing the Finance Cabinet that one of the parcel owners was a state employee and that she did not use her position to influence the negotiation process. Also, it is important to understand that a ROW agent does

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-91: The Kentucky Transportation Cabinet Should Ensure Independence With Right Of Way Employees, And Should Adhere To Established Procedures Regarding The Approval Process Of Right Of Way For State Employees (Continued)

Management's Response and Corrective Action Plan (Continued)

not "set the rate" for which property owners are compensated, the neighboring property owners determine the values through their buying and selling of comparable properties in that area.

In conclusion, the cabinet employee did not actively pursue ownership of Parcel Number (No.) 005 until all avenues of ownership had been explored. It has become general consensus by the district design staff that the cabinet employee and her husband owned Parcel No. 005 since 1990; however, their original source deed was just too vague to determine the true property lines.

The ROW central office failed to submit the parcel batch to the Finance Cabinet for review. The District did submit the required state employee form but it was over looked by the ROW specialist checking the file. It should be noted that the employee responsible does not typically work with agents in the districts directly and did not know the cabinet employee or her husband. Once this oversight was brought to the ROW central office's attention they submitted the information to the Finance Cabinet for their usual approvals and to then forward to the Governor's Office for approval. In an effort to address this situation and to insure that the same action is not repeated, the ROW Director has addressed this situation with the Acquisition Branch staff and we have put in place a new policy that all state employee forms are to be attached at the top of each file to ensure proper processing before payments can be submitted.

This Division has participated in the Office of Inspector General's (OIG) investigation of this acquisition and will continue to cooperate in any further inquiries.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Material Weaknesses and/or Material Instances of Noncompliance:

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards

State Agency: Kentucky Transportation Cabinet

Federal Program: CFDA 20.205 - Highway Planning and Construction

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: \$0

During the FY 2007 audit of Kentucky Transportation Cabinet's (KYTC) schedule of expenditures of federal awards (SEFA), we were not provided a schedule of subrecipients for the Highway Planning and Construction grant (CFDA 20.205) administered by KYTC. Due to this omission, the Commonwealth's SEFA did not disclose amounts sent to subrecipients for this grant for FY 2007. The final revised SEFA presented during the audit of compliance and internal controls over the federal program identified the \$24,188,775 in subrecipient expenditures; however, we were not able to substantiate that total. In addition, KYTC did not identify subrecipients related to this grant in the past several years.

In conducting the audit of the Highway Planning and Construction grant for compliance and internal controls with applicable grant requirements, we were not initially aware of the existence of subrecipients based on the information provided by KYTC during the SEFA procedures and based on a review of the prior year. However, near the end of audit fieldwork, KYTC Chief Audit Executive identified a discrepancy between the KYTC SEFA and a disclosure made in the single audit of another government, indicating the existence of subrecipients for this grant. Upon identifying the discrepancy and investigating the matter internally, KYTC notified the auditor of the error.

Upon being notified of the error, the auditor attempted to obtain the necessary information to assess the materiality of the amounts provided to subrecipients, and determine the status of subrecipient monitoring performed by the two KYTC divisions administering this grant. We requested the FY 2007 schedule of subrecipients to test the monitoring procedures in place over subrecipient expenditures made during the year, and subsequently also requested the FY 2006 schedule of subrecipients for determining which subrecipients identified in the prior year who had single audits were monitored during the FY 2007.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

KYTC was unable to provide a FY 2006 schedule of subrecipients, but did work to provide the FY 2007 schedule of subrecipients. However, our review of the FY 2007 schedule identified that the list was incomplete and inaccurate, having omitted one Metropolitan Planning Organization (MPO) and listing inaccurate expenditures for other subrecipients for one of the two divisions administering the grant. Based on the significance of errors already noted, we did not perform procedures to verify the completeness of the FY 2007 schedule of subrecipients for the other division administering this grant.

We used the schedule provided to review project files for the program's compliance and internal controls over subrecipient monitoring. During the review of these project files it does appear that subrecipient invoices were monitored for allowability during the year. However, the other aspects of subrecipient monitoring are not adequately performed. Our testing identified the following discrepancies:

1. The grant agreements/documentation did not include the CFDA name or number;
2. Quarterly and annual reports were not consistently submitted as required by the grant, and we did not find documentation indicating that the agency followed up with the subrecipients to obtain the missing reports;
3. A formal process of review of the quarterly and annual reports is not in place;
4. There is not a formal policy for requesting subrecipient A-133 single audits, and we identified one subrecipient in our sample with expenditures exceeding \$500,000 that did not submit one;
5. Desk reviews were not on file;
6. Management letters are not being submitted to subrecipients stating the results of desk reviews.

The errors in the schedule of subrecipients occurred because the procedures for compiling the SEFA only includes inquiring of divisions that reported subrecipients in the prior year, rather than requesting subrecipients from all divisions. Also, employee turnover created a strain on employees who were new to the SEFA preparation process since they did not have a historical perspective of the agency's applicable grants and subrecipients.

It also does not appear that each division at KYTC is maintaining its subrecipient list for the grant programs it administers. Without a complete list of subrecipients the divisions cannot guarantee that proper monitoring procedures are being adequately and completely performed.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

As a result, sufficient monitoring procedures were not consistently and systematically performed during the year. Without adequate and timely monitoring, there is an increased risk that subrecipients may fail to comply with applicable grant requirements.

It also came to our attention that Transportation Enhancement projects are being maintained in both the Division of Planning and the Office of Special Programs. If the same types of projects are maintained in different areas of KYTC then inconsistent monitoring procedures could occur because the monitoring responsibilities are not clear-cut.

Because we were unable to complete our testing to determine the accuracy and validity of payments sent to subrecipients, potential questioned cost could exist with the \$24,188,775 sent to subrecipients and not be detected.

OMB Circular A-133 Subpart C, §___.310 (b)(5) states “To the extent practical, pass-through entities should identify in the schedule the total amount provided to subrecipients from each Federal program.”

OMB Circular A-133, Subpart D, §___.400 (d) states, “A pass-through entity shall perform the following for the Federal awards it makes:

1. Identify Federal awards made by informing each subrecipient of CFDA title and number, award name and number, award year, if the award is R&D, and name of Federal agency. When some of this information is not available, the pass-through entity shall provide the best information available to describe the Federal award.
2. Advise subrecipients of requirements imposed on them by Federal laws, regulations, and the provisions of contracts or grant agreements as well as any supplemental requirements imposed by the pass-through entity.
3. Monitor the activities of subrecipients as necessary to ensure that Federal awards are used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements and that performance goals are achieved.
4. Ensure that subrecipients expending \$300,000 (*\$500,000 for fiscal years ending after December 31, 2003*) or more in Federal awards during the subrecipient's fiscal year have met the audit requirements of this part for that fiscal year.
5. Issue a management decision on audit findings within six months after receipt of the subrecipient's audit report and ensure that the subrecipient takes appropriate and timely corrective action.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

6. Consider whether subrecipient audits necessitate adjustment of the pass-through entity's own records.”

Recommendation

We recommend KYTC improve policies and procedures related to the SEFA preparation and related disclosures, especially as it relates to identifying amounts awarded to subrecipients. KYTC should ensure SEFA preparers are adequately trained on internal procedures and the Commonwealth's compilation procedures set forth by the Finance and Administration Cabinet.

We also recommend that KYTC improve its internal controls over subrecipient monitoring by developing comprehensive monitoring policies and procedures, which at a minimum include:

- Review and revise grant agreements to ensure all required elements are communicated to subrecipients, including the CFDA name and number, to ensure the subrecipient is aware of the federal program they are required to comply with;
- Require each division to maintain a list of active subrecipients based on the grant agreements in place, and have the ability to readily identify amounts paid to those subrecipients during the year; with a list of expenditures in each fiscal year to identify which subrecipients exceeded expenditures of \$500,000 that would require an A-133 audit;
- Implement procedures for timely submission of quarterly and annual subrecipient reports per the grant agreement, and implement a KYTC review policy of the quarterly and annual subrecipient reports;
- Implement procedures to ensure the subrecipient A-133 single audits are submitted on a timely basis and document attempts to obtain late single audit reports;
- In the event a subrecipient has not responded timely to a request for audit, consider querying the Federal Award Clearinghouse database to determine if subrecipient A-133 single audits have been completed, and to identify findings that impact KYTC grants, and document this query in the subrecipient files.
- Develop a consistent way to file the audit reports received, file the responses from subrecipients, and file the desk review of the audit reports;

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

Recommendation (Continued)

- Submit a management letter to the subrecipient with the results of the desk review. If corrective action is needed, then KYTC should follow-up in a timely manner;
- Identifying specific sanctions for subrecipients that show a continued inability or unwillingness to have and submit required audit reports, including A-133 single audits.
- Assign responsibility for maintaining and monitoring all like projects, such as Transportation Enhancement projects, to one division to ensure consistency in the tracking and monitoring process.

Management's Response and Corrective Action Plan

KYTC disbursements for FY07 included \$642,853,312 attributed to the CFDA # 20.205 Highway Planning and Construction program. The majority of these transactions were payments to contractors having a vendor relationship with KYTC and \$24,188,775 (3%) was provided to subrecipients.

During the SEFA preparation process, the Division of Accounts (Accounts) sends an email to all areas of KYTC which reported subrecipients in the past requesting a schedule of subrecipients. The responses are then incorporated into the SEFA. As is the case in many agencies, Accounts has experienced a great deal of employee turnover in recent years. In an attempt to ensure the continuation of this key function, Accounts assembled a team to assume the SEFA reporting responsibility. The KYTC SEFA undergoes extensive review within Accounts and it is also reviewed by the Chief Audit Executive before submission. KYTC also relies on APA and the Finance and Administration to identify errors and omissions.

There has not been any formalized SEFA training offered to agencies by either the Finance and Administration Cabinet (FAC) or APA. Consequently, with no significant APA findings or training to the contrary, KYTC for years has reasonably assumed the SEFA report was being produced appropriately. We have contacted FAC and they informed us that they plan to offer SEFA training in a few months; KYTC will participate. As KYTC identified to APA, there were

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

Management's Response and Corrective Action Plan (Continued)

omissions regarding CFDA 20.205. In an attempt to ensure that this type of omission does not occur in the future, Accounts will request subrecipient information from all KYTC offices – not just those known to Accounts as administering federal programs.

The cabinet can and will improve the documentation of subrecipient monitoring and oversight which occurs and incorporate procedures which will enhance this oversight. KYTC feels it is critical to identify best practices which are occurring within the cabinet and standardize those practices within all areas that administer federal funds. All areas have made significant, meaningful improvement in subrecipient oversight over the past five (5) years. Improvements include subrecipient training to Local Public Agencies (LPAs), detailed reimbursement requests, significant supporting documentation requirements, sight visits, etc.

The Chief Audit Executive and the Division of Accounts will develop and implement procedures regarding the KYTC's administration of federal funds to subrecipients and provide training to all areas of KYTC that administer federal funds. This will include the following:

- *Grant agreements will be revised to include the applicable CFDA name, number, name of federal agency and any applicable laws/regulations*
- *Divisions will maintain a database which will identify all subrecipients*
- *The database will be used to track the receipt of required quarterly and annual reports*
- *Subrecipients will be required to provide an OMB A-133 audit or certify that they do not meet the \$500,000 federal fund threshold*
- *KYTC will withhold funding for those subrecipients that do not comply with OMB A-133 audit requirements and quarterly and annual reports*
- *KYTC will conduct desk reviews of all OMB A-133 audits and findings will be communicated to the subrecipient and corrective measures will be tracked and monitored*

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

Management's Response and Corrective Action Plan (Continued)

- *Subrecipient files will contain all required information, audits, and reports*
- *KYTC will provide training to subrecipients to ensure there is full disclosure as to their duties and responsibilities*

KYTC would like to note that of the Division of Planning files reviewed by APA, three were Metropolitan Planning funds and two were earmarked funds—not TE funds. The Division of Planning has not administered TE projects since the program was moved into its own office in 2005. The MPO process is heavily regulated (23 CFR 450) and the oversight requirements are part of those regulations. By law, the Cabinet and the FHWA have substantial involvement in the MPOs daily activities which is documented by meeting minutes. KYTC would also like to note that quarterly and annual reports were consistently provided by MPOs. Subrecipient monitoring was indeed performed, just not documented well.

KYTC does not agree that disbursements to CFDA # 20.205 subrecipients are in question since invoices are scrutinized before payment. We do agree that better documentation of our monitoring procedures, as well as implementing a tracking system for OMB A-133 audits is warranted.

Auditor's Reply

As KYTC is aware, it is their responsibility to provide an accurate and complete list of the subrecipients that received federal money with the SEFA. It is not the responsibility of the APA or the FAC to identify the omissions of subrecipients on the agencies' SEFA, as neither agency is part of KYTC's management nor part of its internal control functions. In reviewing audit reports as far back as 2004, the information relied upon during the KYTC audit included:

1. The subrecipient schedules provided by the agency that did not identify subrecipients for this program;
2. Management representation letters signed by the cabinet secretary that all indicated subrecipient information provided to the auditor for this federal program was complete and accurate;
3. The APA's inquiry of KYTC, as documented in the internal control questionnaires, which did not indicate subrecipient monitoring was being performed for this federal program.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-92: The Kentucky Transportation Cabinet Should Implement Formal Policies And Procedures For Subrecipient Monitoring, And Implement Controls To Ensure Proper Reporting Of Subrecipients On The Schedule Of Expenditures Of Federal Awards (Continued)

Auditor's Reply (Continued)

The APA will very closely monitor this area in the future and will extend procedures to gain additional assurance that subrecipients have been adequately disclosed and monitored.

In regards to the files reviewed by the APA, two KYTC employees, including the Director of the Division of Planning, identified the two projects as TE funds. When asked why this was not maintained in the Office of Special Programs with the other TE funds, they claimed it was because it was an older project and the Division of Planning had already established a relationship with the subrecipient. If the information is incorrect, it is due to an error in the information provided to the auditor.

There is a potential for questioned costs when proper monitoring procedures are not in place. Since the APA was not able to complete testing, we could not conclude that all the disbursements to CFDA #20.205 were accurate and valid payments. We will test KYTC's assertion in future audits once the appropriate information becomes available.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-93: The Kentucky Transportation Cabinet Should Implement Policies And Procedures For Tracking Subrecipients' Audit Reports

State Agency: Kentucky Transportation Cabinet

Federal Program: CFDA 20.600 - State and Community Highway Safety

Federal Agency: U.S. Department of Transportation

Pass-Through Agency: Not Applicable

Compliance Area: Subrecipient Monitoring

Amount of Questioned Costs: \$0

During our review, inquiry, and subsequent testing of Kentucky State Police (KSP) Highway Safety (HS) grant compliance and internal controls over Subrecipient Monitoring, we determined that KSP was noncompliant with subrecipient compliance requirements per OMB Circular A-133. The results of our testing identified the following:

- For the 96 subrecipients for the Highway Safety program, no single audits were received during the FY 2007,
- KSP did not follow up in any manner with the subrecipients of federal funding to comply with the OMB Circular A-133 requirements; therefore, KSP HS personnel were not able to determine if the subrecipient was compliant with federal award requirements, and
- KSP did not maintain a tracking list for the requested audit reports from subrecipients.

Upon discussing our results with KSP HS personnel at the Transportation Cabinet and KSP, they have indicated they are aware of the lack of proper tracking, the non-receipt of audit reports from subrecipients, and the requirement to follow-up on audit report requests in a timely manner.

KSP is noncompliant with subrecipient requirements for FY 2007 as they have not provided the request to the subrecipient regarding the requirement to send in the audits of federal funding, they have not tracked the audits, and they have not followed up with the subrecipients to request audit reports in a timely manner. If the subrecipient does not send the pass-through entity an audit report, and no follow up is performed, then the pass through entity has not been able to determine if the subrecipient has met the federal award and audit requirements.

Agencies receiving federal grants and passing through to other agencies (subrecipients) should develop controls to ensure compliance with subrecipient monitoring requirements per OMB Circular A-133.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-93: The Kentucky Transportation Cabinet Should Implement Policies And Procedures For Tracking Subrecipients' Audit Reports (Continued)

OMB Circular A-133 Part 3, Section M, provides that the pass-through entity should perform the following procedures for compliance with the subrecipient monitoring requirements:

- a) Ensure that the required subrecipient audits were completed, and received.
- b) Issue management decisions on audit findings within 6 months after receipt of the subrecipient's audit report, and
- c) Ensure that subrecipients took appropriate and timely corrective action on all audit findings.

Recommendation

We recommend that KSP HS improve and implement their policies for subrecipient monitoring to include the following:

- Develop a consistent method for requesting audit reports, document the requests, document the follow-up including date and grants manager who initiated it, and maintaining a system of tracking that keeps this information up-to-date so that grants managers know at any point in time the most recent action taken with regards to subrecipient requests and follow up;
- Develop a consistent way to file the audit reports as received, file the responses from subrecipients, and file the review of the audit reports;
- Consider querying the Federal Award Clearinghouse database to determine if subrecipient audits have been completed, identify findings that impact KSP HS grants, and documenting this query in the event a subrecipient has not responded to an audit report request in a timely manner; and
- Identify specific sanctions for subrecipients that show a continued inability or unwillingness to have and submit required audit reports.

Management's Response and Corrective Action Plan

Response from Kentucky State Police:

The Kentucky State Police does not have enough information to neither agree nor disagree with the audit findings listed above regarding subrecipient monitoring for CFDA 20.600. The Kentucky State Police Governor's Office of Highway Safety was the recipient of funding from the National Highway Transportation Safety Administration (NHTSA) under CFDA 20.600 for FY '07 for the time

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-93: The Kentucky Transportation Cabinet Should Implement Policies And Procedures For Tracking Subrecipients' Audit Reports (Continued)

Management's Response and Corrective Action Plan (Continued)

Response from Kentucky State Police (Continued):

period of July 1, 2006-June 15, 2007; however, at such time Executive Order #2007-504 was signed; thereby, transferring the Governor's Office of Highway Safety to the Transportation Cabinet. The Governor's Office of Highway Safety staff, formerly employed by the Kentucky State Police, transferred to the Transportation Cabinet, as well as, all files, documentation, and programs under CFDA 20.600. At such time the Kentucky State Police became a subrecipient of the Transportation Cabinet for funding under CFDA 20.600. In January 2007, prior to this reorganization, the Kentucky Transportation Cabinet Secretary, was appointed as the Governor's Representative for Highway Safety in Kentucky, and a Kentucky State Police Captain remained responsible only for the day-to-day operation of the highway safety program with input from the Secretary of the Transportation Cabinet or his designee (please see attached letter dated January 22, 2007). On February 1, 2007, the signing authority for the Governor's Office of Highway Safety was also transferred from the Kentucky State Police to the Secretary of the Transportation Cabinet. On February 1, 2007, all transactions regarding CFDA 20.600 funding fell under the signing authority of the Transportation Cabinet. For the remainder of FY '07, the Kentucky State Police became a subrecipient of these funds under CFDA 20.600. Additionally in FY '08 the Kentucky State Police has remained a subrecipient of the Transportation Cabinet for funding under CFDA 20.600, and does not administer such programs.

During this audit, Kentucky State Police did not have, nor retain, any files or documentation relating to these awards under CFDA 20.600, other than payroll documentation. Kentucky State Police can not formulate a corrective action plan related to these audit findings as Kentucky State Police remains a subrecipient only, for funding under CFDA 20.600 and does not have any programs under CFDA 20.600 that has subrecipients. Kentucky State Police does not have a direct award relating to these audit findings. Kentucky State Police could not advance any corrective action plans to address this audit finding as Kentucky State Police does not have any authority nor oversight of the Transportation Cabinet nor any programs/awards it oversees.

**COMMONWEALTH OF KENTUCKY
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

FINDING 07-TC-93: The Kentucky Transportation Cabinet Should Implement Policies And Procedures For Tracking Subrecipients' Audit Reports (Continued)

Management's Response and Corrective Action Plan (Continued)

Response from Kentucky Transportation Cabinet:

The Kentucky Transportation Cabinet (KYTC) Office of Highway Safety, Division of Highway Safety Administration will develop and maintain a tracking system that will help ensure compliance with OMB circular A-133 subrecipient audit requirements. This system will include documenting requests for single audits and any follow up taken so that division personnel will know the most recent action taken.

Audit reports received will be forwarded to KYTC Internal Audit Branch for review. After the review a file will be maintained containing all subrecipient audit reports. If follow up is necessary, documentation will be maintained in the file.

When necessary, the KYTC Division of Highway Safety Administration will query the Federal Award Clearinghouse database to assist KYTC in determining if a subrecipient audit has been completed. Since many audits will be conducted by the Auditor of Public Accounts, we will access their database as well.

Subrecipients that continue to fail to respond to our requests for their single audit may have their current grant suspended or terminated and any future requests for funding will not be approved.

Auditor's Reply

During the audit for CFDA 20.600, it was noted that an executive order moved the Highway Safety program from the Kentucky State Police to the Transportation Cabinet effective June 15, 2007. Therefore, we audited the program at KSP and Transportation for FY 07 and responses to this finding were received from both agencies.

THIS PAGE LEFT BLANK INTENTIONALLY

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies</u>					
<i>(1) Audit findings that have been fully corrected:</i>					
FY 06	06-CHFS2-45	The Cabinet For Health And Family Services Should Implement Procedures To Ensure Services Are Received Prior To Paying The Full Contract Amount	93.778	0	Resolved during FY 07.
FY 06	06-CHFS6-6	The Cabinet For Health And Family Services Should Obtain A SAS 70 Audit	93.563	0	Resolved during FY 07.
FY 06	06-CHFS20-46	The Cabinet For Health And Family Services Should Document The Reconciliation Of Quarterly Financial Reports For The Adoption Assistance Program	93.659	0	Resolved during FY 07.
FY 06	06-CHFS21-47	The Cabinet For Health Services Should Ensure Policy And Procedures Are Adhered To And Maintain Adequate Records	93.558	\$18,149	Due to improvements, this finding is downgraded to a control deficiency for FY 07. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 06	06-CHFS22-48	The Cabinet For Health And Family Services Should Maintain Proper Supporting Documentation For Case Files.	93.563	0	Resolved during FY 07.
FY 06	06-CHFS23-49	The Cabinet For Health And Family Services Should Ensure The Jefferson County Child Support Enforcement Office Has Appropriate Approvals For Computer Equipment Purchases	93.563	\$49,604	Resolved during FY 07.
FY 06	06-CHFS24-50	The Cabinet For Health And Family Services Should Ensure Financial Records For Administration Of The Child Support Enforcement Program Remain On-site At The Meade County Attorney Office At All Times	93.563	\$178,511	Resolved during FY 07.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 05	05-CHFS12-43	The Cabinet For Health Services Should Follow Documented Policies And Procedures And Maintain Adequate Records To Ensure Payments Are Made For Services To Eligible Recipients	93.558	\$29,820	Due to improvements, this finding is downgraded to a control deficiency for FY 07. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 05	05-CHFS13-44	The Cabinet For Health And Family Services Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support	93.563	0	Resolved during FY 07.
FY 06	06-COMM1-51	The Commerce Cabinet Should Ensure The New West Branding Contract's Billing Procedures Are Improved	Multiple	\$33,971	Resolved during FY 07.
FY 06	06-DFWR1-52	The Department Of Fish And Wildlife Resources Should Develop Policies And Procedures Overall All Job Duties, Retention Of Accounting Records, And Timely Vendor Payments	15.605 15.611	0	Resolved during FY 07.
FY 06	06-DFWR2-53	The Department Of Fish And Wildlife Resources Should Make Use Of All State Financial Accounting System Components For Proper Administration Of Federal And State Resources	15.605 15.611	0	Resolved during FY 07.
FY 06	06-DFWR3-54	The Department Of Fish And Wildlife Resources Should Implement Its Internal Policies And Procedures Over Vendor Invoice Payments	15.605 15.611	0	Resolved during FY 07.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 06	06-DFWR4-55	The Department Of Fish And Wildlife Resources Should Develop Procedures Requiring Cash Draw Downs Within A Reasonable Time Frame, And Requiring Retention Of Supporting Accounting Records	15.605 15.611	0	Resolved during FY 07.
FY 06	06-DFWR5-56	The Department Of Fish And Wildlife Resources Should Develop Policies And Procedures Over Payroll Errors	15.605 15.611	0	Resolved during FY 07.
FY 06	06-DFWR6-57	The Department Of Fish And Wildlife Resources Should Inform Staff Of Receipt Handling Policies And Implement Policies Requiring Retention Of Accounting Records And Supporting Documentation	15.605 15.611	0	Resolved during FY 07.
FY 06	06-DFWR7-58	The Department Of Fish And Wildlife Resources' Indirect Cost Rates Should Agree To Federally Approved Indirect Cost Rates	15.605 15.611	0	Resolved during FY 07.
FY 05	05-DFWR1-48	The Department Of Fish And Wildlife Resources Should Develop Procedures Over Cash Draw Downs Within A Reasonable Time Frame	15.605 15.611	0	Resolved during FY 07.
FY 05	05-DFWR2-49	The Department Of Fish And Wildlife Resources Should Develop And Implement An Accounting Policy Requiring The Retention Of Supporting Documentation For All Cash And Check Receipts	15.605 15.611	0	Resolved during FY 07.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY05	05-DMA7-56	The Department Of Military Affairs Should Reimburse The Federal Government For Questioned Costs And Request Reimbursement Only For Expenditures That Have Adequate Supporting Documentation	12.401	\$40,188	The federal agency has indicated that they are satisfied that the questioned costs have been resolved.
FY 06	06-DWI8-61	The Department For Workforce Investment Should Ensure Federal Reports Reconcile To The State's Accounting System On A Quarterly Basis By Reporting Category	17.258 17.259 17.260	0	Resolved during FY 07.
FY 06	06-DWI9-62	The Department For Workforce Investment Should Improve Review Procedures Over the Office Of Vocational And Adult Education Consolidated Annual Report Status Of Funds Form	84.048	0	Due to improvements, this finding is downgraded to a control deficiency for FY 07. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 05	05-DW11-59	Information Provided To The Department Of Labor Should Agree With State Accounting Data	84.048	0	Due to improvements, this finding is downgraded to a control deficiency for FY 07. This finding is no longer required to be reported under <i>Government Auditing Standards</i> .
FY 06	06-JUST1-63	The Justice Cabinet Should Implement Procedures To Ensure Subrecipient A-133 Audits Are Submitted Timely	16.575 16.579	0	Resolved during FY 07.
FY 06	06-JUST2-64	The Justice Cabinet Should Implement Procedures For the Timely Submission Of Subrecipient Financial Reports	16.575 16.579	0	Resolved during FY 07.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(1) Audit findings that have been fully corrected (Continued):</i>					
FY 06	05-JUST3-65	The Justice Cabinet Should Implement Procedures To Ensure Consistent Enforcement And Documentation Of Subrecipient Monitoring Requirements	16.575 16.579 16.588	0	Resolved during FY 07.
FY 06	06-TC13-69	The Transportation Cabinet Should Improve Procedures To Ensure The Correct Certification Letter For Materials Is Submitted To The Federal Highway Authority	20.205	0	Resolved during FY 07.
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY 06	06-DMA1-59	The Department of Military Affairs Should Document Costs Charged To The AIOM Tenant Sub-Project, Including An Approved Cost Allocation Plan For Shared Facility Costs	12.401	\$8,003	Corrective action plan implemented, but questioned cost has not been resolved.
FY 06	06-DMA2-60	The Department Of Military Affairs Should Properly Request And Document Grant Extensions	12.401	\$6,335	Corrective action plan implemented, but questioned cost has not been resolved.
FY 06	06-TC12-68	The Transportation Cabinet Should Improve Procedures To Ensure Federal Reports Are Prepared Accurately	20.205	0	See 07-TC-90.
FY 05	05-TC15-71	The Transportation Cabinet Should Ensure All Federal Expenditures Are Allowable	20.205 20.600	\$559,816	Corrective action plan implemented, but questioned cost has not been resolved.
FY 05	05-TC16-72	The Transportation Cabinet Should Improve Procedures To Ensure Federal Reports Are Prepared Accurately	20.205	0	See 07-TC-90.

(3) Corrective action taken is significantly different from corrective action previously reported:

No findings for this section.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(4) Audit finding is no longer valid or does not warrant further action:</i>					
FY 04	04-CFC6-18	The Cabinet For Families And Children Should Maintain Case File Records That Include Client Applications, Recertifications, And Records Of Eligibility Determinations	93.558	\$18,224	Two or more years have passed since the audit report in which this finding was submitted to the Federal Clearinghouse. The Federal Agency is not currently following up on this audit finding. A management decision has not been issued.
FY 04	04-CFC7-19	The Cabinet For Families And Children Should Maintain Adequate Records To Ensure Payments Are Made For Approved And Allowable Goods And Services To Eligible Recipients	93.558	\$16,774	Two or more years have passed since the audit report in which this finding was submitted to the Federal Clearinghouse. The Federal Agency is not currently following up on this audit finding. A management decision has not been issued.
FY 04	04-CFC8-20	The Cabinet For Families And Children Should Only Issue Work Incentive Payments To Eligible Individuals And Should Request And Maintain Adequate Documentation Of The Eligibility Determinations	93.558	\$1,040	Two or more years have passed since the audit report in which this finding was submitted to the Federal Clearinghouse. The Federal Agency is not currently following up on this audit finding. A management decision has not been issued.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(4) Audit finding is no longer valid or does not warrant further action (Continued):</i>					
FY 04	04-CFC10-22	The Cabinet For Families And Children Should Improve Child Support Enforcement Performance To Ensure Children Receive Proper Financial Support	93.563	0	Two or more years have passed since the audit report in which this finding was submitted to the Federal Clearinghouse. The Federal Agency is not currently following up on this audit finding. A management decision has not been issued.
FY 06	06-KHEAA1-65	The Kentucky Higher Education Assistance Authority Should Send Notices To Borrowers Timely	84.032	0	In FY 07, the Commonwealth's component units were not included in the SSWAK report. Follow up on the component unit's prior audit findings should be performed and reported by the public accounting firm conducting their audit.
FY 06	06-KHEAA2-66	The Kentucky Higher Education Assistance Authority Should Be Suborgated To The Federal Government In A Timely Manner	84.032	0	In FY 07, the Commonwealth's component units were not included in the SSWAK report. Follow up on the component unit's prior audit findings should be performed and reported by the public accounting firm conducting their audit.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
<u>Significant Deficiencies (Continued)</u>					
<i>(4) Audit finding is no longer valid or does not warrant further action (Continued):</i>					
FY 06	06-KHESLC1-67	The Kentucky Higher Education Student Loan Corporation Should Closely Monitor Data Transmissions	84.032	\$43,000	In FY 07, the Commonwealth's component units were not included in the SSWAK report. Follow up on the component unit's prior audit findings should be performed and reported by the public accounting firm conducting their audit.
FY 04	04-JUST2-38	The Justice Cabinet Should Provide Sufficient Documentation Of Subrecipient Monitoring Activities	16.575 16.579 16.588	0	Two or more years have passed since the audit report in which this finding was submitted to the Federal Clearinghouse. The Federal Agency is not currently following up on this audit finding. A management decision has not been issued.
FY 04	04-TC11-45	The Transportation Cabinet Should Improve Procedures To Ensure Federal Reports Are Prepared Accurately	20.205	0	Two or more years have passed since the audit report in which this finding was submitted to the Federal Clearinghouse. The Federal Agency is not currently following up on this audit finding. A management decision has not been issued.

**COMMONWEALTH OF KENTUCKY
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

Fiscal Year	Finding Number	Finding	CFDA Number	Questioned Costs	Comments
------------------------	---------------------------	----------------	------------------------	-----------------------------	-----------------

Material Weaknesses/Noncompliances

(1) Audit findings that have been fully corrected:

No findings for this section.

(2) Audit findings not corrected or partially corrected:

No findings for this section.

(3) Corrective action taken is significantly different from corrective action previously reported:

No findings for this section.

(4) Audit finding is no longer valid or does not warrant further action:

No findings for this section.

NOTE: Prior financial statement audit findings are not listed in this schedule. This schedule only lists prior federal awards audit findings.

THIS PAGE LEFT BLANK INTENTIONALLY

APPENDIX

**COMMONWEALTH OF KENTUCKY
APPENDIX
FOR THE YEAR ENDED JUNE 30, 2007**

List Of State Agency Contacts

This report is available on the APA website, www.auditor.ky.gov in pdf format. For other requests, please contact Gregory Giesler, Open Records Administrator, with the APA's office at (502) 573-0050 or gregory.giesler@auditor.ky.gov. If copies of the FY 07 CAFR are required, please contact Jonathan Miller, Finance and Administration Cabinet Secretary, at (502) 564-4240.

The following is a list of individuals by state agency to contact regarding federal award findings listed in the Schedule of Findings and Questioned Costs or the Summary Schedule of Prior Audit Findings.

State Agency	Contact
Cabinet for Health and Family Services	Kelli Hill, Staff Assistant Office of Fiscal Services Cabinet for Families and Health Services 275 East Main Street 4C-C Frankfort, KY 40601 Phone (502) 564-8890 ext. 4336
Department of Fish and Wildlife Resources	Melissa R. Trent Department of Fish and Wildlife Resources #1 Sportman's Lane Frankfort, KY 40601 Phone (502) 5664-7109 ext. 380
Department of Military Affairs	Charles R. Flynn, Chief Administrative Officer Division of Administrative Services Department of Military Affairs Boone National Guard Center 100 Minuteman Parkway, EOC Building Frankfort, KY 40601 Phone (502) 607-1545

**COMMONWEALTH OF KENTUCKY
APPENDIX
FOR THE YEAR ENDED JUNE 30, 2007
(CONTINUED)**

List Of State Agency Contacts (Continued)

State Agency	Contact
Department for Workforce Investment	Tommy Goins, Branch Manager Division of Fiscal Services Department for Workforce Investment 500 Mero Street 2nd Floor Frankfort, KY 40601 Phone (502) 564-3300
Environmental and Public Protection Cabinet	Lisa Cox, Director Division for Administrative Services Environmental and Public Protection Cabinet 500 Mero Street, 4 th Floor Frankfort, KY 40601 Phone (502) 564-2282
Finance and Administration Cabinet	Ed Ross, Controller Office of the Controller Finance and Administration Cabinet Capitol Annex, Room 484 702 Capitol Avenue Frankfort, KY 40601 Phone (502) 564-2210
Office of Homeland Security	Adam Edelen, Executive Director Kentucky Office of Homeland Security 200 Mero Street Frankfort, KY 40601 (502) 564-2081
Transportation Cabinet	Alice Wilson, Chief Audit Executive Office of Budget & Fiscal Management Transportation Cabinet 200 Mero Street Frankfort, KY 40622 Phone (502) 564-4550

